LIBRARY
SUPREME COURT, U. S.

Supreme Court, U.S.
FILED
NOV 22 1971
E. ROBERT SEAVER, CLERK

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1971

No. 71-693

GEORGE GORDON REYNOLDS AND WALTER A. MITCHELL,
*Petitioners,*

*v.*

TEXAS GULF SULPHUR CO. AND CHARLES F. FOGARTY,
*Respondents.*

---

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

---

PARKER M. NIELSON
320 Kearns Building
Salt Lake City, Utah 84101
*Attorney for Petitioner Reynolds*

ROY G. HASLAM
72 East 4th South Street
Salt Lake City, Utah 84111
*Attorney for Petitioner Mitchell*

TABLE OF CONTENTS


| | Page |
|---|---|
| OPINIONS BELOW | 1 |
| JURISDICTION | 2 |
| QUESTIONS PRESENTED | 2 |
| STATUTE AND RULE INVOLVED | 3 |
| Rule 23, Federal Rules of Civil Procedure | 3 |
| 28 U.S.C. §1407 | 4 |
| STATEMENT OF THE CASE | 5 |
| REASONS FOR GRANTING THE WRIT | 9 |
| I CERTIORARI SHOULD BE GRANTED TO IMPLEMENT THE PURPOSES OF THE 1966 AMENDMENTS TO RULE 23, AS AN EXPEDITIOUS METHOD FOR HANDLING A MULTIPARTY CONTROVERSY | 10 |
| A. *The Trial Judge's Narrow Application of the Elements of the Rule Restricts Its Utility* | 10 |
| B. *The Lower Courts Inflexible Handling of These Equity Proceedings Conflicts With Decisions of This Court* | 11 |
| C. *Certiorai Should be Granted to Avoid Duplicity* | 13 |
| D. *The Court of Appeals' Decision Conflicts with the Foundational Decision of the Court of Appeals for the Seventh Circuit* | 15 |
| E. *The Court of Appeals' Decision Conflicts with Time Honored Decisions of this Court concerning Class Actions* | 17 |
| F. *Strict Application of Res Judicata Frustrates the Advisory Committee's Intent* | 19 |

TABLE OF CONTENTS (Continued)

II THE WRIT SHOULD BE GRANTED TO INSURE AN EXPANSIVE USE OF THE JUDICIAL PANEL ON MULTI-DISTRICT LITIGATION ..... 21

III THE DECISION CONFLICTS WITH THIS COURT'S RECENT PRONOUNCEMENTS CONCERNING RECOVERY OF COSTS OF CONDUCTING THE ACTION ..... 22

CONCLUSION ..... 25

APPENDIX ..... 1a

CASES CITED

Astor v. Texas Gulf Sulphur Company, 306 F. Supp. 1333 (S.D.N.Y., 1969) ..... 9

Cannon v. Texas Gulf Sulphur Company, 47 F.R.D. 60 (S.D.N.Y. 1969) ..... 9, 11

Cannon v. Texas Gulf Sulphur Company, 65 Civ. 1223 (S.D.N.Y., February 10, 1971) ..... 7

Cannon v. Texas Gulf Sulphur Company, 65 Civ. 1223 (S.D.N.Y., March 8, 1971) ..... 8

Cannon v. Texas Gulf Sulphur Company, CCH FED. SEC. L. REP. ¶93,071 (S.D.N.Y., June 8, 1971) ..... 8, 9

Cannon v. Texas Gulf Sulphur Company, 323 F. Supp. 990 (S.D.N.Y., February 5, 1971) ..... 9

Dolgow v. Anderson, CCH FED. SEC. L. REP. ¶93,249 (E.D.N.Y., October 21, 1971) ..... 20

Fink v. Coates, 323 F. Supp. 988 (S.D.N.Y., February 5, 1971) ..... 8, 9

Frieman v. Texas Fulf Sulphur Company, CCH FED. SEC. L. REP. ¶91,627 (D. Ill. 1965) ..... 10

TABLE OF CONTENTS (Continued)

Hansberry v. Lee,
311 U.S. 32 (1940) ..... 18

J.I. Case Co. v. Borak,
377 U.S. 426 (1964) ..... 24

Kline v. Burke Construction Corp.,
260 U.S. 226 (1922) ..... 12

Mills v. Electric Auto Lite Co.,
396 U.S. 375 (1970) ..... 23, 24

Mitchell v. Texas Gulf Sulphur Co.,
446 F. 2d 90 (10th Cir. April 26, 1971) ..... 9

Partridge v. Martin,
102 F. 2d 284 (8th Cir.) *cert. denied* 307 U.S.
644 (1939) ..... 12

Reynolds v. Texas Gulf Sulphur Co.,
309 F. Supp. 548 (D. Utah 1970) ..... 9

Reynolds v. Texas Gulf Sulphur Co.,
309 F. Supp. 566 (D. Utah 1970) ..... 9

SEC v. Coates,
CCH FED. SEC. L. REP. ¶92,251 (2d Cir. 1968) *cert.*
*denied* 394 U.S. 976 (1969) ..... 9

SEC v. Texas Gulf Sulphur Co.,
446 F. 2d 1301 (2d Cir. June 10, 1971) ..... 9

SEC v. Texas Gulf Sulphur Co.,
258 F. Supp. 262 (S.D.N.Y. 1966) ..... 9

SEC v. Texas Gulf Sulphur Co.,
401 F. 2d 833 (2d Cir. 1968) ..... 9

SEC v. Texas Gulf Sulphur Co.,
312 F. Supp. 77 (S.D.N.Y. 1970) ..... 9

Smith v. Swormstedt,
16 How. [57 U.S.] 288 (1853) ..... 10, 18

Sprague v. Ticonic National Bank,
307 U.S. 161 (1939) ..... 23

Supreme Tribe of Ben Hur v. Cauble,
255 U.S. 356 (1921) ..... 18, 20

Taylor v. Salmon,
4 Myl. & Cr. 134 (1838) ..... 18

Texas Gulf Sulphur Co. v. Ritter (Petitioner Reynolds,
real party in interest), 371 F. 2d 145 (10th Cir. 1967) ..... 9

Weeks v. Bareco Oil Co.,
125 F. 2d 84 (7th Cir. 1941) ..... 16

AUTHORITIES CITED

ABA SPECIAL COMMITTEE ON AVAILABILITY OF LEGAL SERVICE, RECOMMENDATIONS TO THE HOUSE OF DELEGATES, August 1966 ..... 9

CALVERT, A TREATISE UPON THE LAW RESPECTING PARTIES TO SUITS IN EQUITY, (2d Ed. 1847) ..... 18

CHAFFEE, SOME PROBLEMS OF EQUITY,
(1950) ..... 14, 17, 18, 23, 24

Kalven & Rosenfield, *The Contemporary Function of the Class Suit*, U. CHI. L. REV. 684 (1941) ..... 15, 21

Keefe, Levy & Donovan, *Lee Defeats Ben Hur*,
33 CORN. L.Q. 327 (1941) ..... 11, 19

1 MOORES FEDERAL PRACTICE Pt. 2 p. vii. ..... 10

RESTATEMENT OF JUDGMENTS §86 Comment h ..... 20

Weinstein, *Revision of Procedure: Some Problems in Class Actions*, 9 BUFFALO L. REV. 433 (1960) ..... 21

## Statutes and Rules Cited


15 U.S.C. §78j ..... 5

28 U.S.C. §1254(1) ..... 2

28 U.S.C. §1407 ..... 4, 9, 21, 22

17 C.F.R. 240.10b-5 ..... 5

Rule 23, Federal Rules of Civil Procedure ..... 3, 21

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1971

## No.

---

GEORGE GORDON REYNOLDS AND WALTER A. MITCHELL,

*Petitioners,*

*v.*

TEXAS GULF SULPHUR CO. AND CHARLES F. FOGARTY,

*Respondents.*

---

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

---

Petitioners George Gordon Reynolds and Walter A. Mitchell, plaintiffs, appellees and cross-appellants in the courts below, pray that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Tenth Circuit herein.

## OPINIONS BELOW

The opinion of the United States District Court for the District of Utah on the merits is reported at 309 F. Supp. 548 and set fourth at page 1a of the Appendix to this Petition. The opinion of the District Court denying the class action is reported at 309 F. Supp. 566 and set forth at page 36a of the Appendix to this petition. The opinion of the Court of Appeals is re-

ported at 446 F.2d 90 and is reproduced at page 49a of the Appendix to this Petition.

## JURISDICTION

The judgment of the Court of Appeals was entered on April 26, 1971. A timely petition for rehearing was denied on September 10, 1971. The jurisdiction of this Court is invoked under the provisions of Title 28 U.S.C. §1254 (1). The time for filing this Petition expires December 9, 1971.

## QUESTIONS PRESENTED

In a case involving proliferated claims based upon a common question simultaneously asserted by hundreds of persons in several different districts of the United States, affecting the interests of thousands of defrauded shareholders in a single public corporation:

1. Whether the purpose of the Advisory Committee on Federal Rules, to effect economies and efficiences in the judicial process and assure prompt and effective relief to litigants, was frustrated by the lower courts' restrictive reading of revised Rule 23, Federal Rules of Civil Procedure?

2. Whether judicial economies should have been achieved by referring parallel proceedings simultaneously conducted in two separate districts to the Coordinating Committee on Complex and Multi-Party Litigation?

3. Whether substantive rights of parties before the court and absentee class members were denied by a refusal to permit class action proceedings, where an action on any other basis is not economically feasible?

4. Whether plaintiffs who establish a violation of the securities laws by their corporation, and the "common questions" controlling suits by others, should be reimbursed for the costs of establishing the violation, costs of expert witnesses and legal expenses, and if so in what manner?

## STATUTE AND RULE INVOLVED

The pertinent provisions of Rule 23, Federal Rules of Civil Procedure (Rule) and the statutory provisions involved, are as follows:

Rule 23, Federal Rules of Civil Procedure:

> (a) PREREQUISITES TO CLASS ACTION. One or more members of a class may sue or be sued as representative parties on behalf of all only if (1) the class is so numerous that joinder of all members is impracticable, (2) there are questions of law or fact common to the class, (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and (4) the representative parties will fairly and adequately protect the interests of the class.
>
> (b) CLASS ACTIONS MAINTAINABLE. An action may be maintained as a class action if the prerequisites of subdivision (a) are satisfied, and in addition:
>
> * * *
>
> (3) the court finds that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy. The matters pertinent to the findings include: (A) the interest of members of the class in individually controlling the prosecution or defense of separate actions; (B) the extent and nature of any litigation concerning the controversy already commenced by or against members of the class; (C) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; (D) the difficulties likely to be encountered in the management of a class action.
>
> * * * *
>
> (d) ORDERS IN CONDUCT OF ACTIONS. In the conduct of actions to which this rule applies, the court may make appropriate orders: . . . (4) requiring that the pleadings be amended to eliminate therefrom allegations as to representation of absent persons, and that the action proceed accordingly; . . . The orders may be combined

with an order under Rule 16, and may be altered or amended as may be desirable from time to time.

28 U.S.C. §1407:

(a) When civil actions involving one or more common questions of fact are pending in different districts, such action may be transferred to any district for coordinated or consolidated pretrial proceedings. Such transfers shall be made by the judicial panel on multidistrict litigation authorized by this section upon its determination that transfers for such proceedings will be for the convenience of parties and witnesses and will promote the just and efficient conduct of such action. Each action so transferred shall be remanded by the panel on or before the conclusion of such pretrial proceedings to the district from which it was transferred unless it shall have been previously terminated: *Provided, however,* That the panel may separate any claim, cross-claim, counter-claim, or third party claim and remand any of such claims before the remainder of the action is remanded.

(b) Such coordinated or consolidated pretrial proceedings shall be conducted by a judge or judges to whom such actions are assigned by the judicial panel on multidistrict litigation. For this purpose, upon request of the panel, a circuit judge or a district judge may be designated and assigned temporarily for service in the transferee district by the Chief Justice of the United States or the chief judge of the circuit, as may be required, in accordance with the provisions of chapter 13 of this title. With the consent of the transferee district court, such actions may be assigned by the panel to a judge or judges of such district. The judge or judges to whom such actions are assigned, the members of the judicial panel on multidistrict litigation, and other circuit and district judges designated when needed by the panel may exercise the powers of a district judge in any district for the purpose of conducting pretrial depositions in such coordinated or consolidated pretrial proceedings.

(c) Proceedings for the transfer of an action under this action may be initiated by –

(i) the judicial panel on multidistrict litigation upon its own initiative, or

(ii) motion filed with the panel by a party in any action in which transfer for coordinated or consolidated pretrial proceedings under this section may be appropriate. A copy of such motion shall be filed in the district court in which the moving party's action is pending.

## STATEMENT OF THE CASE

On April 13, 1964, Texas Gulf Sulphur Company (TGS), acting by and through its Executive Vice President, Respondent Fogarty, published a statement discounting rumors concerning its mineral explorations near Timmins, Ontario, Canada (deceptive release). The rumors had reportedly leaked out because of large purchases of TGS stock by insiders, which had caused a flurry of trading on the stock exchange. Three days later, on April 16, 1964, TGS issued a second press statement confirming the discovery of a mine at Timmins, which has since proven to be one of the most spectacular mining discoveries in history (corrective release). All of the essential information contained in the April 16 release was based upon exploration which had been completed prior to when the deceptive release was prepared, and a materially significant portion of it had been available to TGS since November of 1963.

Petitioners were shareholders in TGS who read the deceptive release and sold their stock on the morning of April 16, before the corrective release was communicated to them or was reasonably available to members of the investing public. In the wake of the disclosure that the deceptive release misstated and omitted mention of material facts, within the meaning of the anti-fraud provisions of federal securities laws,[1] which became known when the United States Securities and Exchange Commission (SEC) initiated enforcement proceedings against TGS and its management, more than 500 TGS shareholders initiated upwards of 100 separate suits (App. 40a) in many different

[1]Principally, Rule 10b-5 (17 C.F.R. 240.10b-5) adopted pursuant to section 10 of the Securities Exchange Act of 1934 (15 U.S.C. §78j).

district courts affecting rights in 691,400 TGS shares sold by more than a thousand persons (App. 37a-38a). Many, like Petitioner Mitchell, brought suit individually, but many others, like Petitioner Reynolds, alleged that they were seeking relief on behalf of a class composed of all persons similarly situated.

These proliferated lawsuits quickly became centered in two forums. The Reynolds-Mitchell suits became centered in the District of Utah (Utah court), where they progressed with expedition through discovery, trial, and appeal on the merits, resulting in judgments in favor of the plaintiffs. A significantly larger number of suits were lodged in the Southern District of New York (New York court) where they have remained stalled for upwards of seven years in pretrial proceedings, with no resolution of the merits yet in the offing.

The Utah court entered two separate orders pursuant to Rule 23(d) striking Reynolds' class allegations on February 6, 1967 and October 13, 1967, respectively, and then proceeded to a trial on the merits commencing April 29, 1968. In the meantime, proceedings in New York had been suspended by stipulation of counsel, and neither discovery nor proceedings on the class allegations had been conducted. The Utah court announced its opinion resolving the merits in favor of the plaintiffs on October 17, 1969, and 23 days later the New York court ordered—for the first time and then only provisionally—that the cases lodged there would proceed as a class action and in a subsequent statement from the bench indicated that a substantial reason was the fact that the Reynolds-Mitchell cases had established the probability that liability was present. On November 20, 1970—after the Reynolds-Mitchell cases had been fully briefed and a scant 12 days before they were submitted for decision on appeal—the New York court submitted notice under Rule 23(c) advising the absentees for the first time that an action had been commenced in New York, but making no mention of the Reynolds-Mitchell cases.

Before judgment was entered in the trial court, Reynolds moved a third time for a *proper* determination under the Rule,

and stressed that the earlier orders had not addressed themselves to the elements the Rule specifies must be considered and that in any event Rule 23(d) permits modifications "as may be desirable from time to time." In making this third application Reynolds was supported by some of the plaintiffs from New York, who intervened to urge that the Utah proceedings were the most advantageous to the class members because, among other reasons, they had progressed by a period of years in advance of the New York cases. The third effort resulted in a published opinion dated January 13, 1970, in which Judge Ritter recited his original ruling, inferred that despite Reynolds repeated efforts over a three year period he had not been sufficiently diligent in asserting the question, and deferred to the New York proceedings. App. 36a.

Reynolds was then joined by absentee members of the class who had learned of his judgment, and they jointly sought intervention in the New York proceedings while Reynolds' appeal was pending. They alleged that their addition as parties would improve the representation within the meaning of Rule 23(d) and they suggested, as Reynolds had previously done in the Court of Appeals, that the Judicial Panel on Multi-District Litigation should be employed to secure the advantages of proceedings conducted in *both* forums to the absentee class members. Judge Bonsal, in a pique which is part of the printed record,[2] then rejected all such requests, directed that the issues already tried in the Reynolds case would be retried to a jury in his court, entered an order declaring the New York plaintiffs the *only* proper class representatives and limiting the class members who joined with Reynolds to *merely* appearing (*i.e.* they were not even permitted to file papers with the court), and then severely restricted membership in the class so that persons whose circumstances were most like those of Reynolds and Mitchell were excluded and presumptively declared

---

[2]See hearing before Judge Bonsal in Cannon v. Texas Gulf Sulphur Co., 65 Civ. 1223 (S.D.N.Y.) on February 10, 1971. Judge Bonsal evi-

*not* to even have a cause of action. On March 26, 1971 and November 3, 1971, the New York court entertained motions to revoke the class determination altogether, on the theory that despite the outstanding Reynolds-Mitchell judgments there was no substantial possibility that plaintiffs similarly situated could prevail. If these motions are granted, the entire group of absentees will be deprived of any forum in which to assert their claims.

The Utah judgment, along with the denial of the class action, was affirmed by the Court of Appeals. Thus, the curiosity of a Utah action, with liability sans class, and a New York action with class sans liability, is the product, and Reynolds—who has obtained a judgment which will certainly benefit all of the shareholders under the doctrines *stare decisis* and collateral estoppel—is declared *not* to be a proper class representative and those similarly situated with him have effectively had summary judgment entered against them. At the same time, others—the New York plaintiffs who have consented to a seven year delay while Reynolds and SEC have actually litigated the rights of the class—are declared by fiat to be the *only* proper class representatives[3] even though the cause of substantially more than half of the class membership has been effectively abandoned.[4]

---

dently viewed the intervention as an interference with the processes of his court. *Cf. Fink v. Coates*, 323 F. Supp. 988, 989-90 (S.D.N.Y., February 5, 1971) where Judge Bonsal inferred that the Utah judgment was not well reasoned. Judge Bonsal suggested that Reynolds lawyers, who had conducted the trial on the merits and the appeal, did not desire to protect the class, but were greedily attempting to establish their right to a fee.

[3]See Cannon v. Texas Gulf Sulphur Co., 65 Civ. 1223 (S.D.N.Y. order filed Mar. 8, 1971).

[4]*C.f.* Cannon v. Texas Gulf Sulphur Co., CCH FED SEC. L. REP. ¶93,071 (S.D.N.Y. June 8, 1971).

## REASONS FOR GRANTING THE WRIT

With our judicial system at its very breaking point, with scandalous delays in the time required to bring a legitimate controversy to a resolution on the merits forcing the public to examine the alternatives to the judiciary as a method of resolving conflicts, the lower courts have ignored procedures which could have reversed the trend and helped restore public confidence. While the academic community and Bar Associations decry the phenomenon in which high court costs and free legal services for the poor combine to leave middle-class America *without* meaningful access to our courts[5] and permit those who are financially endowed, such as Respondent corporation, to manipulate or engineer interminable delays while the costs of litigation take their natural toll of the infinitely less powerful plaintiffs, the lower courts have squandered an opportunity for an enlightened application of the 1966 amendments to Rule 23 and the 1968 amendments to the Judicial Code (28 U.S.C. §1407) which would have provided effective relief for the "middle Americans" who are the members of the class, and significantly shortened the duration of this litigation. The opportunity thus lost may not easily be recovered, for the circumstances of this case, which have already resulted in at least fifteen reported opinions,[6] are already a classic example of

---

[5]*E.g.* ABA SPECIAL COMMITTEE ON AVAILABILITY OF LEGAL SERVICE, RECOMMENDATIONS TO THE HOUSE OF DELEGATES, August 1966.

[6]SEC v. Texas Gulf Sulphur Co., 446 F.2d 1301 (2d Cir. June 10, 1971); Mitchell v. Texas Gulf Sulphur Co., 446 F.2d 90 (10th Cir. April 26, 1971); SEC v. Coates, CCH. FED SEC. L. REP. ¶ 92,251 (2d Cir. 1968) *cert. denied* 394 U.S. 976 (1969); SEC v. Texas Gulf Sulphur Co., 401 F.2d 833 (2d Cir. 1968); Texas Gulf Sulphur Co. v. Ritter (Petitioner Reynolds, real party in interest) 371 F.2d 145 (10th Cir. 1967); Fink v. Coates, 323 F. Supp. 988 (S.D.N.Y. February 5, 1971); Cannon v. Texas Gulf Sulphur Co., 323 F. Supp. 990 (S.D.N.Y., February 5, 1971); Cannon v. Texas Gulf Sulphur Co., CCH FED SEC. L. REP. ¶ 93,071 (S.D.N.Y., June 8, 1971); SEC v. Texas Gulf Sulphur Co., 312 F. Supp. 77 (S.D.N.Y. 1970); Reynolds v. Texas Gulf Sulphur Co., 309 F. Supp. 548 (D. Utah 1970); Reynolds v. Texas Gulf Sulphur Co., 309 F. Supp. 566 (D. Utah, 1970); Astor v. Texas Gulf Sulphur Co., 306 F. Supp. 1333 (S.D.N.Y. 1969); Cannon v. Texas Gulf Sulphur Co., 47 F.R.D. 60 (S.D.N.Y. 1969); SEC v. Texas Gulf Sulphur Co., 258 F. Supp.

a complex multi-district suit which is destined to remain a guiding influence under Rule 23 for a considerable time to come.

This Court should grant certiorari to determine if we shall have a judiciary for just the elite, or if methods recently devised to remedy the defects of our system shall be implemented.

## I

## CERTIORARI SHOULD BE GRANTED TO IMPLEMENT THE PURPOSES OF THE 1966 AMENDMENTS TO RULE 23, AS AN EXPEDITIOUS METHOD FOR HANDLING A MULTI-PARTY CONTROVERSY

### A. *The Trial Judge's Narrow Application of the Elements of the Rule Restricts Its Utility.*

> If the administration of justice by the courts is to endure, the Bench and Bar must devise and employ new procedures which will increase the efficiency and improve the quality of justice without increasing the burden on litigants. 1 MOORES FEDERAL PRACTICE Pt. 2 p. vii.

The 1966 amendments to Rule 23 were designed to overhaul the "common issue" class action, a common law equity device which American jurisprudence has struggled to perfect for over a hundred years.[7] These amendments thus represent one of a precious few recent innovative devices designed to improve the efficiency and the quality of justice. Regrettably, since its adoption the revised Rule has enjoyed a shaky history, for even the occasional statements to the effect that the Rule should be applied liberally have failed to grasp the fundamental purpose of the Rule to streamline the judiciary and have focused on its purely mechanical incidents. Worse, is the tendency of many courts to view this type of class action as an oppressive device, or as a method for solicitation of large claims by plain-

---

262 (S.D.N.Y 1966); Frieman v. Texas Gulf Sulphur Co., CCH FED. SEC. L. REP. ¶ 91,627 (D. Ill. 1965).

[7]One of the earliest authorities is Smith v. Swormstedt, 16 How [57 U.S.] 288 (1853)

tiffs lawyers. These conceptual errors are evident in this case, and if not corrected they could well impair the value of the revised Rule.

The lower courts did not rest their decision on any alleged factual inadequacy, and to the contrary, it was subsequently determined that the elements of the Rule were present. See *Cannon v. Texas Gulf Sulphur Company*, 47 F.R.D. 60 (S.D. N.Y. 1969). Indeed, it was quite clear that Judge Ritter's original ruling was the result of (1) his belief that the New York courts would proceed with expedition and (2) his desire to avoid the administrative burdens of this complex multiple controversy:

> THE COURT: I am not very happy about getting a lawsuit in here with 691,000 shares of stock involved with all of those potential—high numbers of shareholders all over the country, maybe international, too—transactions. Tr. 24

The trial judge's final published opinion did not reconsider the matter, or examine the policy of the Rule in light of the ensuing events which had proven the earlier ruling to be in error, but simply attempted to justify the earlier ruling. The Court of Appeals glossed over the issue when it declined to even consider whether the Advisory Committee's concept of a streamlined procedure had been subverted, and justified its result with the cryptic conclusion that an "abuse of discretion" had not been shown. This Court should, therefore, grant certiorari to establish standards for the implementation of the Rule which will effectuate its objectives.

B. *The Lower Courts Inflexible Handling of These Equity Proceedings Conflicts With Decisions of This Court.*

> [I]s it not much fairer to society as a whole – the group that pays the bills for long-drawn-out and costly litigation —to settle as much as possible in a single suit? Keefe, Levy & Donovan, *Lee Defeats Ben Hur*, 33 CORN. L.Q. 327, 343 (1948).

The trial judge's fundamental assumption was that there could be but one class action, but there is no language in the Rule which requires or even suggests such a purpose, and to the contrary, it frustrates the plain purpose of the Advisory Committee to promote expedition and efficiency. As the circumstances of this case illustrate, it cannot be projected in advance which of two parallel proceedings will most effectively achieve their common goal, and for that reason the courts should not undertake to do so.

Moreover, the trial judge's assumption conflicts with this Court's holding that in proceedings in equity the "controversy is not a thing, and a controversy of a mere question of liability does not involve the possession or control of a thing . . . . Each court is free to proceed in its own way and in its own time, without reference to the proceedings in the other court." *Kline v. Burke Construction Corp.*, 260 U.S. 226, 230 (1922). The Court of Appeals for the Eighth Circuit has also held that one member of a class does not acquire the exclusive right to sue, or to prevent other class suits, by merely starting a suit and alleging that it is for the benefit of all having similar claims. *Partridge v. Martin*, 102 F. 2d 284, 288 (8th Cir.) *cert. denied* 307 U.S. 644 (1939). Surely the interests of judicial efficiency and the fortunes of the absentee members of the class would be better served if *both* actions were permitted to proceed, at least on a provisional basis, for unanticipated factors such as the evident reluctance of the New York counsel in this case to proceed aggressively with litigation, may demonstrate that an initial impression was not correct. The Advisory Committee evidently shared that view, for it provided that *all* class action orders were to be provisional.[8] Indeed, it may even develop that both proceedings can serve a useful function in resolving different aspects of a complex dispute, and where two proceedings are being conducted in any event, as they were in this case, no added burden is imposed on the judiciary by entering pro-

[8] See subdivisions (c) (1) and (d) of the Rule.

visional orders such as the Rule prescribes. By rejecting that approach the lower courts have read an inflexibility into the Rule which was never intended.

Viewed at the threshold, it was perhaps reasonable for Judge Ritter to accept the assurances of Respondents that the New York actions were more advanced and would proceed with expedition, but after subsequent events had proven the reverse to be true what merit was there in attempting to justify the earlier errors? The New York action was not even declared to be a class action until after the Reynolds case had been tried, and even then only provisionally under an order subject to modification at any time before the decision on the merits. But after Reynolds had already tried and determined the common *issue*, which is all that the class action is concerned with, it was simply beyond question that the fortunes of the class and the ends of judicial efficiency would be better served with him as their representative, particularly when it is considered that Judge Ritter was deferring to a forum in which the class representatives appeared most unlikely to be successful in protecting the absentees rights.[2] "Abuse of discretion," even if it were the appropriate inquiry, must comprehend such a subversion of the absentees rights.

C. *Certiorari Should Be Granted to Avoid Duplicity.*

> The King of Brogdignag gave it for his opinion that, "whoever could make two ears of corn, or two blades of grass to grow upon a spot of ground where only one grew before, would deserve better of mankind, and do more essential service to his country than the whole race of politicians put together." In matters of justice, however, the benefactor is he who makes one lawsuit grow where two grew

---

[2]See App. 37a, where Judge Ritter recited that Judge Bonsal "ruled that such conduct of defendants did not violate the provisions of . . . Rule 10b-5." Yet, Judge Ritter had simultaneously ruled that the defendants conduct *did* violate Rule 10b-5, and every other Court to consider the question has agreed with him. Thus, Judge Ritter was apparently forcing the absentees to seek redress in a forum where it appeared that their claims would be rejected.

> before . . . Questions of law or fact which would otherwise be tried over and over can by this means be determined once for all in a single proceeding. This avoidance of multiplicity of suits saves the parties from needless expense and vexation, economizes the time of judges and jurymen, and frees the dockets for the affairs of other litigants. CHAFFEE, SOME PROBLEMS OF EQUITY, 149 (1950).

The Advisory Committee's sweeping 1966 revisions of Rule 23 relied heavily upon the prescient writings of Chancellor Zechariah Chaffee, Jr., *supra*, and others which are liberally quoted herein. The lower courts thwarted the Advisory Committee, however, by *mandating* that multiple lawsuits should sprout and vex the federal courts with duplicate trials—how many one can but speculate—for years to come.

If the Court of Appeals displayed lack of insight in permitting redundant lawsuits, the New York court compounded the error by further condemning the class to the "needless expense and vexation" Chancellor Chaffee had reference to. Thus, though Reynolds had already tried the common issue and resolved that aspect of the case in favor of the absentee class members, the New York court proposed to submit that same issue to a new trial, this time before a jury, with the attendant threat that the common issue might then be resolved adversely to the interest of the absentees. The degree of vexation the absentees were subjected to became evident when Reynolds approached the New York counsel directly with an invitation for them to join in an effort to merge the two actions and thereby extend the benefits of the Reynolds judgment to their own clients and all of the absentees—which was rejected in favor of an effort to employ the Utah judgment as leverage to force a settlement on terms substantially less favorable to the absentees[10] (who remain uninformed of the *Reynolds* case). The

[10]In a letter to counsel for Reynolds dated December 18, 1970, counsel in the New York proceedings declared:

> Dick [Richard Dannenberg] tells me that Judge Bonsal is still pressing for a settlement even before the disposition of your 10th Circuit case.
>
> . . . . .
>
> Our feeling, from the conferences with Judge Bonsal, is that he

Rule's requirements of notice and Court approval of any proposed settlement, and provision for improvement of class representation, seem designed to protect the absentees from such practices.

D. *The Court of Appeals' Decision Conflicts with the Foundational Decision of the Court of Appeals for the Seventh Circuit.*

> [T]here is by no means complete symmetry between binding the defendant to a favorable decree and binding the absentee to an unfavorable decree. Clearly, the defendant has been afforded his day in court; he has had the opportunity to present his case fully in his own right, and he has lost. He has no more reason to litigate the entire controversy against the absentee members than he has to do so against the immediate plaintiff. . . . The defendant cannot properly complain about the way in which he is treated; he can complain only that the absentees are not also subjected to the risk of losing the case. Kalven & Rosenfield, *The Contemporary Function of the Class Suit*, 8 U. CHI. L. REV. 684, 713 (1941).

The cardinal transgression of the lower courts was their failure to recognize and implement the foregoing principle, for the trial judge implicity assumed that Reynolds' third effort to obtain a proper class ruling could not be entertained because it was made after the trial (but before the "decision on the merits"). That the Advisory Committee intended to to adopt a more liberating philosophy is evident in its approving citation of the Kalven & Rosenfield writings.

The trial judge quite mistakenly declared that "what the

---

> would just as soon not complicate the posture of the case and the possibility of settlement at this time by adding another dimension to the array of lawsuits already filed with him, at least not in this stage of the proceedings. . . . This may be shooting craps a bit; but it seems to be our best position at present.

The letter is attached as an exhibit to Petitioner Reynolds Motion to File Supplementary Brief in the Court of Appeals, and was also filed with Judge Bonsal in February 1971, in connection with the effort of appearing class members to improve the class representation.

revisionists of this rule had in mind was to *limit* these class actions," (emphasis added) (Tr. 5) viewing what the Advisory Committee had advanced as a hopeful judicial reform as a corrupt device for solicitation (Tr. 23). The Court of Appeals simply ignored the problem by declaring that the policy of the Advisory Committee was merely a collateral issue (App. 79a), and placed its decision on a supposed absence of a showing of abuse of discretion.

Surely the rights of the absentees, and Reynolds, to a speedy, efficient and economical determination of their rights cannot be considered "collateral," for the Advisory Committee clearly undertook to elevate these considerations to the status of substantive rights. That purpose is fairly certain from the frequent reference to *Weeks v. Bareco Oil Co.*, 125 F. 2d 84, 90 (7th Cir. 1941):

> To permit the defendants to contest liability with each claimant in a single, separate suit, would, in many cases give defendants an advantage which would be almost equivalent to closing the door of justice to all small claimants. This is what we think the class suit practice was to prevent. Like many another practice, necessity was its mother. Its correct limitations must be ascertained by the experiences which brought it into existence. . . . If the defense is to create barriers, and to make litigation expensive, so as to *avoid* trial, the opposition by defendants to a single trial can better be understood and appreciated. Such a position does not appeal to the chancellor, who wants to know the truth, and to fix liabilities on the basis of the true facts.

By opting for Respondents' position, in which trials are proliferated through an application of the ethics of the casino (*i.e.*, one should not win unless he also runs the hazard of losing) the Court of Appeals not only turned its back on the enlightened approach of the Advisory Committee in which judicial efficiency is considered paramount to such illusory concepts of mutuality, but also adopted a position in conflict with that of the Court of Appeals for the Seventh Circuit. Moreover, the

lower courts ignored that the class action had been alleged consistently, for a long period prior to trial, and was thus not an after the fact effort by Reynolds in any sense. Respondents vigorously defended the case with full knowledge of Reynolds' claims of class representation, and there is no reason to assume that their conduct of the trial would have been more vigorous if the case had been provisionally declared to be a class action. Certiorari should be granted to establish that the policy of the Rule is not to be subverted by procedures such as were indulged in by the lower courts.

E. *The Court of Appeals' Decision Conflicts with Time Honored Decisions of this Court Concerning Class Actions.*

> If a mighty wind swept away all the bills of peace cases yet decided and dispelled the atmosphere of unreality that hovers about this subject, so that we could make a fresh start, we should never set up formulae about privity, community of interest, and general property right. Everybody would accept the general principle admirably stated by Judge Woolsey: "... the avoidance of multiplicity of suits by every device, which is jurisdictionally possible and practically convenient, should be encouraged and should be one of the main objectives of procedural administration, and of decisions by courts in practice cases." Then we should go on to examine the available methods of handling a multiple controversy, and the practical policies which should influence a judge in choosing among these methods.
>
> What prevents our making this fresh start now? Even if the doctrine of *stare decisis* has any proper application to a procedural problem of this sort, there is excellent authority, as we have seen; for taking the attitude suggested. CHAFFEE, SOME PROBLEMS OF EQUITY, 183 (1950).

To say the least, the lower courts handling of this question was unimaginative. To say more, it was genuinely destructive of what is possibly the most desperate need of contemporary jurisprudence.

The result is that the lower courts have pressed the modern penchant for literal due process beyond the limits of practical

logic. Common law equity jurisprudence knew no such formalism, and recognized the duty of the court "to adapt its practice . . . to the existing state of society," [11] and that "if . . . the only consideration is a persons connection with a certain interest, the purpose of justice may be accomplished in his absence," [12] particularly where the courts "had already heard whatever was worth saying." [13]

This Court adopted these principles more than a century ago in *Smith v. Swormstedt*, 16 How. [57 U.S.] 288, 302-3 (1853) when it was held that a "common issue" suit by a few may be binding on the rights of many, provided the suit is fairly conducted. *Supreme Tribe of Ben Hur v. Cauble*, 255 U.S. 356 (1921) reaffirmed that doctrine, and held that *res judicata* may be applied *even to those who were not before the court*, if representation was adequate.[14] These, it would appear, are *substantive* rights which the Advisory Committee intended to secure. The revised Rule was designed to give the absentee class members a chance to indicate if they considered the representation to be adequate, within the meaning of this Court's decisions, and not to limit the use of class actions as the trial judge assumed. Nothing in the amended Rule, or in the Advisory Committee notes, reveals an intent to retreat from over a century of equity jurisprudence as exemplified in these holdings of this Court.

The absentees right to notice, and an election with respect to the Reynolds suit was thus denied. It is not, of course, necessary for the court to give notice simply because a complaint is filed alleging a class action, but the Rule does suggest, if not clearly declare, that if the elements specified by the Rule are satisfied the absentees have a right to notice of all matters important to an individual choice to participate or "opt out."

---

[11] Taylor v. Salmon, 4 Myl. & Cr. 134, 141-2 (1838).

[12] CALVERT, A TREATISE UPON THE LAW RESPECTING PARTIES TO SUITS IN EQUITY, 22-23 (2d Ed. 1847).

[13] CHAFFEE, SOME PROBLEMS OF EQUITY, 211-220 (1950).

[14] *Cf.* Hansberry v. Lee, 311 U.S. 32, 42 (1940).

This Court should declare that right to be one which may not be denied for arbitrary reasons.

F. *Strict Application of Res Judicata Frustrates the Advisory Committee's Intent.*

> But granting that there exist in the law examples of distinctions based on differences among jural relationships, does it necessarily follow that we must make distinctions on this basis as to the binding effect of class suit judgments? In other words (and without essaying facetiousness), granting that a black dog can be distinguished from a white one, the distinction is of no force when the necessity of obtaining a dog license arises. Is there not danger of falling into an attitude of unthinking formalism, like that of the old common law, when we start assuming that all legal distinctions are meritorious in and of themselves and forget that they should be constantly examined in the light of the purpose they were originally drawn to serve? Keeffe, Levy & Donovan, *Lee Defeats Ben Hur*, 33 CORN. L.Q. 327, 334 (1948).

Yet, the lower courts fell into just such unthinking formalism, for they assumed that when the Advisory Committee undertook to prescribe a jural relationship which would guarantee the availability of *res judicata* (*viz.*, the notice procedures of subdivision (c) (3) of the Rule[15]), it also intended to overrule the prior decisions of this court in cases where such a jural relationship was not established. We may concede that if subdivision (c)(3) had been invoked the judgment's effect as a matter of *res judicata* would be better defined. But does it follow that because the trial judge erred and did not invoke

---

[15]Pertinent provisions of subdivision (c) of the Rule are as follows:
(3) The judgment in an action maintained as a class action under subdivision (b)(1) or (b)(2), whether or not favorable to the class, shall include and describe those whom the court finds to be members of the class. The judgment in an action maintained as a class action under subdivision (b) (3), whether or not favorable to the class, shall include and specify or describe those to whom the notice provided in subdivision (c)(2) was directed, and who have not requested exclusion, and whom the court finds to be members of the class.

subdivision (c) (3) procedures the judgment may *not* have *res judicata* effect? The Advisory Committee notes categorically reject such an interpretation:

> [S]ubdivision (c) (3) does not disturb the recognized principle that the court conducting the action cannot predetermine the *res judicata* effect of the judgment; this can be tested only in a subsequent action.

The "recognized principle" adverted to is obviously the *Ben-Hur* line of authorities. If there could be any doubt that the Advisory Committee so intended, its citation of RESTATEMENT OF JUDGMENTS §86 Comment h. (1942) renders its meaning clear:

> If, however, the conduct of the proceedings is proper, it is immaterial that the other members of the class were not given notice or did not know of the existence of the action.

Patently, the Advisory Committee did not intend to overrule those authorities, and could not do so even if it had.

Respondents urged in the lower courts, *inter alia*, that the Advisory Committee *had* overruled the *Ben Hur* line of authorities, and that the language of Rule 23(d) permitting orders "striking" class allegations to be "altered or amended *as may be desirable from time to time*" (emphasis added) was therefore a mistake, for it was intended that such orders could be altered or amended only "before the decision on the merits." Compare subdivision (c)(1) of the Rule. Putting aside the fact that *all three* of Reynolds class action motions were made "before the decision on the merits" (*viz.*, before entry of judgment), the merit of the distinction proposed is nevertheless rendered academic by the recent decision of Judge Weinstein in *Dolgow v. Anderson*, CCH FED. SEC. L. REP. ¶93,249 (E.D.N.Y. October 21, 1971). Judge Weinstein held, while dismissing the class aspects of a case which he had previously determined to be a class action, that "[s]hould the individually named plaintiffs ultimately prevail . . . the court could then consider re-instatement of the class action." *Id.* at page 91,537. Thus,

even if Respondents were correct—which seems improbable under the significantly different language of the two subsections—Reynolds should have been permitted to pursue his class action, for he asked Judge Ritter to do exactly what Judge Weinstein held that he should have done. Moreover, Judge Weinstein's views should be accorded great weight, for he was one of the architects of the Rule.[16]

To require such a strict adherence to *res judicata* is to vitiate the purpose of the common question class action, for then "the rule is reduced to saying that where it is impracticable to bring all the parties before the court they must nevertheless be brought before the court." [17]

## II

## THE WRIT SHOULD BE GRANTED TO INSURE AN EXPANSIVE USE OF THE JUDICIAL PANEL ON MULTI-DISTRICT LITIGATION

Petitioners urged on appeal that the provisions of 28 U.S.C. §1407 dealing with coordination of multi-district litigation should be applied to avoid the unfortunate results of this case.[18] These provisions have never been construed by this Court. They, like Rule 23, represent creative efforts to modernize a creaky judicial system, and this case presents a unique opportunity to breath life into these provisions.

---

[16]Judge Weinstein, who was then a professor of law at Columbia, is the author of Weinstein, *Revision of Procedure: Some Problems in Class Actions*, 9 BUFFALO L. REV. 433 (1960) which was cited liberally and relied upon by the Advisory Committee.

[17]Kalven & Rosenfield, *The Contemporary Function of the Class Suit*, 8 U. CHI. L. REV. 684, 700 (1941).

[18]There is a conceptual problem in that 28 U.S.C. 1407 deals *exclusively* with pre-trial proceedings, but it is *only* a conceptual problem, for if the class action ruling were reversed there would, indeed, be pretrial "proceedings" (*viz.*, class action proceedings) yet to be conducted in the *Reynolds* case, even though it has been determined on the merits. Reference to pretrial proceedings, rather than to *cases* at pretrial stage, would admit the construction urged by Petitioners.

The opinion of the Court of Appeals contains no reference to Petitioners urging for solution of the problem by reference to the Multi-District Panel, though that is an appropriate solution to the dilemma. Title 28 U.S.C. §1407(b) even permits the designation of a judge to serve in the transferree district. Failure to invoke these procedures resulted in further delays to the absentee class members.

## III

## THE DECISION CONFLICTS WITH THIS COURT'S RECENT PRONOUNCEMENTS CONCERNING RECOVERY OF COSTS OF CONDUCTING THE ACTION

A mythical Lilliputian visitor would surely marvel at a judicial system which could produce the curiosities of this case. Reynolds and Mitchell, in a literal sense, are forced to play the role of a private attorney general. The beneficiaries of their services are the public, which obtains the cleansing effect of exposure of fraud conducted in the market place and the formulation of legal standards to deal with the unique problems which are presented, and the absentee class members, whose benefit is a direct pecuniary one.

In a "common question" class action such as this one, where an individual's stake is modest[19] when compared with the enormous economic power of his opponents, the plaintiff cannot effectively litigate his rights without the strength of numbers. Thus, the availability of the class action rises to the status of substantive right—for *both* the representative and the absentee class members.

The notes to subdivision (b)(3) of the Rule indicate that it was designed by the Advisory Committee to be read in that manner, for the Advisory Committee declared that the Rule is to "achieve economies of time, effort and *expense*" (emphasis

---

[19]Reynolds total interest amounts to $12,000, while the interest of the class is, at a minimum, $14,000,000 (App. 75a-76a). Reynolds' expert witness fees alone, without regard for legal fees, will largely deplete his judgment. R. 740.

added). The fundamental purpose of subdivision (b)(3) to avoid expense becomes crystal clear when it is considered that the Advisory Committee's *sole* citation to the foregoing statement was CHAFFEE, SOME PROBLEMS OF EQUITY 201 (1950):

> Hence it was far cheaper and more convenient to have a single suit in chancery, which was accustomed to handle polygonal controversies . . . . it was an obvious waste of time to try the common question of law and fact over and over in separate actions . . . . It was much more economical to get everybody into a single chancery suit and settle the common questions once and for all. . . .
>
> From such a bill of peace it was a natural step to a representative suit. The very identity of interests which made it easy to bring everybody in, also made it somewhat superfluous to do so.
>
> If the claims of A,B,C, and D were exactly like those of E,F,G, and H, and if A,B,C, and D were stout fellows, would not they be able to say all that could be said for E,F,G, and H as well on their own behalf?

Reynolds and Mitchell have surely demonstrated that they are such "stout fellows." No reason is evident why the absentees should be required to suffer the expense of duplicating their efforts, or why they should be required to bear those expenses alone.

This Court has recognized this policy in cases which are very similar to class actions. Thus, in *Mills v. Electric Auto Lite, Co.*, 396 U.S. 375 (1970) it was held that where a party establishes a violation of the securities laws which has the effect of benefiting a large group of shareholders similarly affected, the plaintiff should be "reimbursed . . . for the costs of establishing the violation." [20] The *Mills* case is thus an en-

---

[20] The rationale, which is an expansion of earlier precedent concerning situations in which the plaintiffs efforts result in the establishment of a "fund" *Sprague v. Ticonic National Bank*, 307 U.S. 161, 166 (1939), was that "to award attorneys' fees in such a suit to a plaintiff who has succeeded in establishing a cause of action is not to saddle the unsuccessful party with the expenses but to impose them on the class that has benefited from them and that would have to pay them had it brought suit." 396 U.S. 375 at 396.

largement of the doctrine of *J. I. Case Co. v. Borak*, 377 U.S. 426, 433 (1964); where this Court taught that "it is the duty of the courts to be alert to provide such remedies as are necessary to make effective the congressional purpose."

The relationship of these propositions to the substantive rights of Reynolds, Mitchell and the absentee class members is simple and direct. If society cannot devise methods to assure that those in Reynolds and Mitchell's position may recover their outlay, suits by those in their position will quickly disappear, for Reynolds' modest $12,000 stakes does not justify such exorbitant costs. The rights of thousands of absentees, and policy considerations vital to the public, hang in the balance, for without persons such as Reynolds who are willing to champion the cause of a faceless multitute the interests of the absentees will be lost by default.

Under any concept of the class action, the absentee holders of 691,400 shares are benefited by Reynolds and Mitchell's actions within the meaning of this Courts *Mills* decision. Respondents reply in the lower courts that Reynolds *chose* to pursue his own class action rather than assume the position of a non-appearing class member in the New York proceedings is not persuasive, for there was no class action in New York at the time of Reynolds' trial. Moreover, the fundamental assumption in class proceedings is that the representative *will* be self appointed. Even if there had been a New York class action at the time, the Rule nevertheless assumes that if a class member is convinced that those managing a suit will do so badly, or for any other reason is dissatisfied with the representative proceedings, he may improve the representation or even initiate his own action.[21]

---

[21] CHAFFEE, SOME PROBLEMS OF EQUITY, 230 (1950):

> Furthermore, although the unnamed members of a class may have no constitutional rights to a day in court, considerations of fairness still survive. Surely, in the future, common decency requires some sort of steps to be taken to apprise people that litigation is under way which seriously affects their life insurance policies or other financial expectations. They ought to be in-

The wisdom of that construction is evident if one considers the position of the absentee class members. Without Reynolds' self-appointed efforts, there would be no judgment today. Moreover, if Reynolds had not volunteered the efforts necessary to properly resolve the common issues, and had lost, can there be any doubt that TGS would have proposed the adverse Reynolds judgment as a bar to the New York proceedings?

The attitude of Judge Bonsal, when Reynolds joined with other absentee class members in seeking intervention in New York to secure the benefits of his adjudication of the common issues to the class, was destructive of these ends. The trial judge is the guardian of the class interest, and his practice should be adapted to proposals such as Reynolds advanced which would secure the absentees rights. Moreover, as Reynolds made clear in his attempted intervention and has made clear herein, he did not consider himself engaged in a sort of race with the New York plaintiffs or in any sense in competition with them, and Judge Bonsal took too narrow a view of the matter when he suggested that Reynolds proposed to supplant, duplicate or denigrate the efforts of the New York court. But if, as this court has declared, a proceeding in equity is viewed as a controversy and not a thing, no reason is apparent why two different proceedings in two different courts, may not simultaneously resolve different phases of the same controversy. If they do, no reason is apparent why the efforts of either court should be duplicated, which is all that Reynolds suggested in his New York intervention.

## CONCLUSION

The task of improving the quality and efficiency of justice in the United States is one which commends the energy of this Court. This case presents an exceptionally good vehicle for the

---

formed as well as represented. They ought to have some notion of what is going on, some chance to see whether the actual parties in the case are doing a competent job. What sort of lawyers have they engaged? How hard are they fighting? Will more money help, and how much?

achievement of these goals because of the restrictive handling of the class action and multi-district problems by the lower courts. Moreover, the result, in which Reynolds and Mitchell have been denied recovery for expenses incurred for the benefit of the entire stockholder group, and the absentee class members have been denied the benefits of the Reynolds-Mitchell judgment, illustrate the maladies of the system in microcosm. Because of the extraordinary publicity which has been given this case, it is very possibly the most appropriate vehicle for the accomplishment of judicial reform which could be proposed.

Respectfully submitted,

PARKER M. NIELSON
320 Kearns Building
Salt Lake City, Utah 84101
*Attorney for Petitioner Reynolds*

ROY G. HASLAM
72 East 4th South Street
Salt Lake City, Utah 84111
*Attorney for Petitioner Mitchell*

## INDEX TO APPENDIX


| | PAGE |
|---|---|
| Opinion of the District Court (Decided January 9, 1970) | 1a |
| Class Action Opinion of the District Court (Entered January 13, 1970) | 36a |
| Judgments of the District Court (Entered January 13, 1970) | 44a |
| Opinion of the Court of Appeals (Decided April 26, 1971) | 49a |
| Judgment of the Court of Appeals (Entered April 26, 1971) | 81a |
| Order of the Court of Appeals Denying Petition for Rehearing (Dated September 10, 1971) | 82a |

## Opinion of the District Court
## (Dated January 9, 1970)

UNITED STATES DISTRICT COURT

DISTRICT OF UTAH, CENTRAL DIVISION

---

**C-62-67**

WALTER A. MITCHELL,

*Plaintiff,*

*v.*

TEXAS GULF SULPHUR COMPANY, a Texas Corporation, and CHARLES F. FOGARTY,

*Defendants.*

---

**C-132-66**

GEORGE GORDON REYNOLDS,

*Plaintiff,*

*v.*

TEXAS GULF SULPHUR COMPANY, a Texas Corporation, and CHARLES F. FOGARTY,

*Defendants.*

---

**C-54-67**

ARTHUR R. STOUT, JR., and MARY LOUISE STOUT, Wife,

*Plaintiffs,*

*v.*

TEXAS GULF SULPHUR COMPANY, a Texas Corporation, and CHARLES F. FOGARTY,

*Defendants.*

---

RITTER, C. J.

Common to all four cases, which were consolidated for trial, are alleged violations of Sec. 10(b) of the Securities and Exchange Act of 1934[1] and Rule 10b-5 promulgated by the Securities and Exchange Commission.[2] One complaint includes a count in common law fraud, another alleges a conspiracy between the defendants to violate Sec. 10(b) and Rule 10b-5. Another complaint alleges violations by defendants of affirmative fiduciary duties to disclose inside information, and alleges violations of Sec. 9 of the Securities and Exchange Act of 1934.[3] The cases have been tried upon the theory of violations of Sec. 10(b) and Rule 10b-5. The other claims have not been pressed. Recovery of damages under the theory of violations of Sec. 10(b) and Rule 10b-5 precludes recovery of further damages in any event.

After the actions were filed, defendants filed an original action with the United States Court of Appeals for the Tenth Circuit under its Rule 28, seeking a writ of prohibition to restrain the trial judge from proceeding to try the actions, and a writ of mandamus directing the trial judge to (a) set aside his order denying petitioners' motion to transfer the cases to the United States District Court for the Southern District of New York under 28 U.S.C. Sec. 1404 (a), (b) transfer the cases as to defendant Texas Gulf Sulphur Co., and (c) either dismiss the action as to defendant Charles F. Fogarty or, in the alternative, transfer the case as to such defendant to the New York Federal Court.[4] The Court of Appeals, without making any final

1. 15 U.S.C. Sec. 78j(b).

2. 17 C.F.R. 240.10b-5.

3. 15 U.S.C. Sec. 78i.

4. Texas Gulf Sulphur, et al. v. The Honorable Willis W. Ritter, et al., 371 F.2d 145 (1967).

determination of facts necessary to prove venue, refused to issue either a writ of prohibition or a writ of mandamus, and upheld the action of the trial judge in overruling the motion attacking venue. The court stated that as to the corporate defendant venue and process are good "because, without dispute, it transacts business in Utah." As to both the individual defendant, Fogarty, and the company, the court held venue will lie in the Utah district "if any of the acts or transactions complained of took place in that district" and, further, that if "venue lies in Utah for that reason, valid process may be had upon Fogarty personally 'in any other district of which the defendant is an inhabitant or wherever the defendant may be found.'" Fogarty's preparation and issuance of a press release to representatives of financial firms and newspapers for transmission over instrumentalities of interstate commerce to branch offices and newspapers throughout the country, which press release plaintiffs contend violated Sec. 10(b) and Rule 10b-5, is sufficient to satisfy requirements of venue and service of process as to defendant Fogarty in three of the four actions. Defendants contend that as to the fourth action there is no venue or proper service of process on Fogarty because the plaintiff in that action sold his stock in December, 1963, several months before issuance of the press release, and because none of the acts or transactions complained of took place in the Utah District.

JURISDICTION

Jurisdiction as to all parties exists (a) under 28 U.S.C. Sec. 1331, the amount in controversy in each of the consolidated cases being in excess of $10,000.00, exclusive of interest and costs, and there being necessary diversity of citizenship between the parties in each case, and (b) by virtue of the allegations in each case of violations of provisions of Sec. 10(b) of the federal statute and S.E.C. Rule 10b-5.

*Appendix —Opinion of the District Court*

FACTUAL BACKGROUND

In November, 1963, Texas Gulf Sulphur Co. (herein sometimes "TGS") core drilled an anomaly[5] near Timmins, Ontario, Canada, which had been detected during the course of an aerial and ground geophysical survey program. The drilling of this hole[6] was completed November 12, 1963, at a depth of 655 feet. Visual examination of the core by the company's chief geologist, Walter Holyk, indicated an average copper content of 1.15%, and an average zinc content of 8.64% over a length of 599 feet. The core was split longitudinally and one-half was sent to a Utah assay house for chemical analysis. The chemical assay proved that the visual appraisal was uncommonly accurate. It disclosed an average mineral content of 1.18% copper, 8.2% zinc, and 3.94 ounces of silver per ton over a length of 602 feet.

The visual appraisal of the core prompted the company to take steps to improve its position without waiting for the chemical assay. The anomaly tested by this hole included lands to which the company did not at the time have the mineral rights, and TGS concluded that additional tracts of adjoining land should be acquired. Immediate action was taken to maintain secrecy as to the results of the first hole. The president of the company issued an order that no one outside of the exploration group[7] should be told of the prospect, the drill camp was moved to another site, all signs of drilling activity were removed and the drill site was camouflaged by standing cut saplings in the snow.

5. An area where there are variations in electrical conductivity, from normal background, of underlying rock formations.

6. The initial hole was on what was known as the Kidd-55 segment of land. It was designated K-55-1. Subsequent holes were designated K-55-2, K-55-3, etc.

7. The information was even withheld from other officers, directors and employees of TGS.

A second hole was intentionally drilled off of the anomaly to divert attention from Kidd-55-1, and the barren core was left lying on the ground near K-55-2.

The importance of the findings based on the core from the first test hole was indicated by a Memorandum for the Files, prepared November 14, 1963, by the company's chief geologist, in which the statement was made that this drill hole "intersected significant copper and zinc mineralization throughout the entire cored length of 655 feet." The author of the memorandum noted that the intersection was "obviously of ore grade" but he warned against "extrapolating this intersection to tonnage estimates" and pointed out that it would be impossible to estimate the true width of the sulphide zone until a second drill hole was directed across the intersection from west to east. The first hole had been drilled from east to west. He concluded the memorandum with the observation that efforts should be made to acquire adjoining lands through purchase or option agreements.

TGS acquired three additional 160-acre tracts adjacent to the site of the initial drill hole—one in December, 1963, another in February, 1964, and the third on March 27, 1964.[8] Drilling was resumed on March 31, 1964, when drill hole K-55-3 (in reality the *second test hole* because K-55-2 was intentionally drilled off of the anomaly) was commenced. It was started 510 feet west of K-55-1 and was drilled in an easterly direction at a 45 degree angle so as to cross

8. Defendant's Exhibit P-2 includes photostat copy of a story that appeared in the April 17, 1964 issue of the Wall Street Journal relative to the press conference held April 16, 1964, at which TGS announced its "major strike". The story quotes Claude O. Stephens, president of TGS, as stating that Texas Gulf's "land position is favorable" and further that "Texas Gulf holds the mineral rights in 70% of Kidd township and has substantial acreage in adjacent townships." The Wall Street Journal story also reported that another TGS official had estimated that TGS had options, claims or ownership of about 60,000 acres in the area.

K-55-1 in a vertical plane. It was completed by 7:00 p.m. April 7, 1964.[9] Visual appraisal of the core of K-55-3 compared very favorably with both the visual appraisal and the chemical assay of the core of the first drill hole. The visual examination of the third core indicated an average mineral content of 4.12% copper and 7.93% zinc over 641½ feet of its 876-foot length. This core eliminated the chance that K-55-1 had been drilled "down-dip" and established generally the east and west margins of the sulphide ore-body.

Test hole K-55-4 was started 200 feet *south* of K-55-1 and was drilled from east to west at a 45-degree angle in a vertical plane parallel to the vertical plane of the first hole. It was completed by 7:00 p.m., April 10. Again, visual examination of the core indicated significant mineralization—mineral content of 1.14% copper and 8.24% zinc for 366 feet of its 579-foot length. The significance of the date and time—April 10, 7:00 p.m.—lies, first, in the admission by defendants that although its press release of Sunday, April 12, purported to reflect the results of drilling "done to date" it actually was based upon drilling information as of the evening of April 10, and, second, in the contention of plaintiffs that even upon the basis of information available on the evening of April 10, the press release was inaccurate and misleading.

By 7:00 p.m. on April 10 some drilling had been done in holes K-55-5 and K-55-6. K-55-5 was started on April 10 at a point 200 feet *north* of K-55-1, and was slanted westerly at an angle of 45 degrees in a vertical plane parallel to an assumed plane containing K-55-1 and K-55-3. At 7:00 p.m. that evening substantial copper mineralization had been encountered over the last 42 feet of this hole's length

9. Because of the importance of events occurring between March 31 and April 16, 1964, particular dates and times are of special significance.

at that time, which was 97 feet. K-55-6 was started on April 8, two days before the start of K-55-5, at a point 300 feet *easterly* of K-55-1. It was drilled in a westerly direction at an angle of 60 degrees, and was intended to explore mineralization *beneath* K-55-1. By the evening of April 10, substantial copper mineralization had been encountered over the last 127 feet of the hole's length, which at that time was 569 feet.

Between the evening of April 10 and the morning of April 13, when the press release information was published substantial copper mineralization had been encountered in K-55-5 to the 580-foot mark, an additional 483 feet of mineralization since the evening of April 10, and visual estimates of the core indicated an average mineral content of 0.82% copper and 4.2% zinc over a 525-foot length. At that time K-55-6 had been drilled to the 946 mark and had encountered mineralization. Two more holes, K-55-7 and K-55-8, were commenced on April 12 and 11, respectively. K-55-8 was a broader hole drilled for the purpose of obtaining a core that could be used in metallurgical tests of the amenability to milling of the materials encountered.

*Rumors in Canada and New York*

Although the company had treated the first test hole as "tight", rumors began to spread shortly after the first of the year 1964, and there was considerable excitement in Timmins and Toronto about a reported discovery. By early April, 1964, there was a "tremendous staking rush going on", according to the testimony of Richard D. Mollison, TGS vice president in charge of exploration, and lands within several miles of the area had been staked. People were watching all surface traffic, and low-flying planes passed over the area several times a day. Silence and secrecy on the part of TGS and its officials were not effective to curb widespread rumors and speculation in Canada and later in New York.

*Appendix —Opinion of the District Court*

On April 9, 1964, the Toronto Globe and Mail published a story in which it was stated that "Rumors that one of the biggest copper deposits in North America has been discovered near Timmins have Bar Street agog", and that in the past two weeks the Toronto Stock Exchange "has been experiencing its wildest speculative spree since the Nineteen Fifties." The Toronto Daily Star on the same day stated that rumors had gained ground "of a major copper strike about 10 miles North of Timmins by Texas Gulf Sulphur Co." On April 10 the Toronto Globe and Mail reported that speculative mining fever still gripped the Toronto stock market "as officials of Texas Gulf Sulphur Co. of New York maintained a tight-lipped silence on what —if anything—they have discovered in Northern Ontario."

The rumors spread to the United States and on the morning of Saturday, April 11, 1964, both the New York Times and the New York Herald Tribune carried stories about the rumored discovery. The Times story referred to an unverified rumor that TGS "had made a sensational copper strike" that had caused "feverish activity in penny speculatives on the Toronto market," and to a reported surge of staking in various townships flanking Timmins, and to hotels and motels bulging with prospectors and would-be prospectors. The story in the Herald Tribune in part reported:

> The biggest ore strike since gold was discovered more than 60 years ago in Canada has stampeded speculators to the snowbound old mining city of Timmins, Ontario, some 450 miles northwest of Toronto.
>
> This time it's copper * * *
>
> The story of the strike goes something like this: Texas Gulf Sulphur has been active in the Big Water area, accessible only by airplane, for several years. The richness of the copper it discovered was so great

that samples reportedly were flown out of the country to be assayed.

The huge lode is supposed to consist of a bed of copper sulfite (sic) 600 feet wide with a possible overall copper return of 2.87 per cent through most of its width. This yield, in itself, is considered rich in mining circles.

But the richest yield comes from the first 100 feet of that 600-foot belt. It is supposed to be 5.6 per cent, a bonanza if the story proves more than just a myth. But myth it may be * * *

The story of the strike reportedly leaked out when it was discovered that certain employees of Texas Gulf Sulphur were buying into the company's stock * * *

*Press Release of April 12*

With the appearance of the Times and Herald Tribune stories TGS decided to issue a press release. The president of the company, Claude O. Stephens, directed the executive vice president, Charles F. Fogarty, to prepare the release. After consulting with public relations advisers, legal counsel, the vice president in charge of exploration, and others, the following statement (quoted in pertinent part) was given to newsmen and representatives of financial publications in the late afternoon or early evening of April 12:

"New York, April 12—The following statement was made today by Dr. Charles F. Fogarty, Executive Vice President of Texas Gulf Sulphur Company, in regard to the company's drilling operations near Timmins, Ontario, Canada. Dr. Fogarty said:

" 'During the past few days, the exploration activities of Texas Gulf Sulphur in the area of Timmins, Ontario, have been widely reported in the press, coupled with rumors of a substantial copper discovery

there. These reports exaggerate the scale of the operations, and mention plans and statistics of size and grade of ore that are without factual basis and have evidently originated by speculation of people not connected with TGS.

"'The facts are as follows. TGS has been exploring in the Timmins area for six years as part of its overall search in Canada and elsewhere for various minerals—lead, copper, zinc, etc. During the course of this work, in Timmins as well as in Eastern Canada, TGS has conducted exploration entirely on its own, without the participation of others.

"'Numerous prospects have been investigated by geophysical means and a large number of selected ones have been core-drilled. These cores are sent to the United States for assay and detailed examination as a matter of routine and on advice of expert Canadian legal counsel. No inference as to grade can be drawn from this procedure.

"'Most of the areas drilled in Eastern Canada have revealed either barren pyrite or graphite without value; a few have resulted in discoveries of small or marginal sulphide ore bodies.

"'Recent drilling on one property near Timmins has led to preliminary indications that more drilling would be required for proper evaluation of this prospect. The drilling done to date has not been conclusive, but the statements made by many outside quarters are unreliable and include information and figures that are not available to TGS.

"'The work done to date has not been sufficient to reach definite conclusions and any statement as to size and grade of ore would be premature and possibly mis-

leading. When we have progressed to the point where reasonable and logical conclusions can be made, TGS will issue a definite statement to its stockholders and to the public in order to clarify the Timmins project * * *."

Plaintiffs contend that the foregoing press release is inaccurate, incomplete, misleading and deceptive. Defendants take the position that it was accurate at the time it was prepared and issued. Before discussing the contentions of the parties with respect to the press release we call attention to a few more facts.

*Public Announcements of Major Strike on April 16*

On the day that the information contained in the foregoing press release was published—Monday, April 13—a reporter for The Northern Miner, a Canadian mining industry journal, by invitation visited the properties near Timmins, inspected the drill cores and conferred with TGS officials, including its chief geologist and its vice president in charge of exploration. Around the first of April, approximately 12 days prior to the press release, Mr. G. M. Ackerley, a reporter with The Northern Miner, had been orally invited by a vice president of TGS to visit the properties on April 20, 1964, for the purpose of preparing an article. This oral invitation was confirmed by a letter dated April 6 from vice president Richard D. Mollison, who testified that he gave Ackerley the invitation in response to repeated requests from him "and because of all the wild rumors and wild statements that were already so prominent in that district, and with my expectation that three weeks' time, three weeks of drilling, would throw some light on what there was and he could come up then at the end of that three weeks and see what it was." A meeting of the stockholders of TGS had been scheduled

for April 23. Mr. Mollison further testified that because of the development of the rumors in Canada and New York they decided to invite Mr. Ackerley to come a week earlier.

On the basis of what he saw and heard on April 13, Mr. Ackerley prepared an article which, in accordance with previous understanding, he submitted to Mr. Mollison for him to hold until the company was ready to release the same. Mr. Mollison made an insignificant change by adding some names of exploration department personnel and on April 15 returned the article to Mr. Ackerley for publication. It was published on the morning of April 16, the same day that TGS notified the press in New York that it had made a major strike. In pertinent part Mr. Ackerley's article read:

> "Texas Gulf Sulphur has chalked up a brilliant exploration success * * * a major new zinc-copper-silver mine is definitely in the making * * *.
>
> "* * * on the basis of seven tests either completed or drilling it can be stated that a strike length of 600 ft. minimum has been established showing an ore width of roughly 300 ft. which has been traced so far to a maximum vertical depth of about 800 ft. * * * this must be recorded as one of the most impressive drill holes completed in modern times.
>
> "For a core length of a shade better than 600 ft., the hole averaged in excess of 1% copper, 8% zinc, and nearly four ounces of silver.
>
> "And there are impressive, strong sections within this width which in themselves are quite spectacular. In the upper part of the hole, for example, a core length of 82 ft. ran 7.1% copper, 9.7% zinc, and 2.4 ozs. silver. And still deeper, a strong zinc section of better than 100 ft. averaged out to in excess of seven ounces of silver in addition to ore-grade zinc values * * *.

"From the dimensions already known, the Northern Miner can say that something in excess of 10,000,000 tons of ore is indicated. It is capped with something like 20 ft. of overburden, presenting no stripping problems, and the steep dip and wide widths will lend themselves ideally to an open-pit mining situation.

"The picture should unfold rapidly at this stage, but officials emphasize that it is still at the embryo point * * *"

On April 16, TGS announced to the press a strike of at least 25,000,000 tons of ore. A prepared release was read to representatives of the press and of financial publications at 10:00 A.M., and summaries of the announcement appeared on the private wire services of Merrill, Lynch, Pierce, Fenner and Smith and of Dow Jones within the hour. In part this release read:

"Texas Gulf Sulphur Company has made a major strike of zinc, copper and silver in the Timmins area of Ontario, Canada. * * *

"Seven drill holes are now essentially complete and indicate an ore body of at least 800 feet in length, 300 feet in width and having a vertical depth of more than 800 feet * * *

"This is a major discovery. The preliminary data indicate a reserve of more than 25 million tons of ore. The only hole assayed so far represents over 600 feet of ore, indicating a true ore thickness of nearly 400 feet * * *

"Visual examination of cores from the other holes indicates comparable grade and continuity of ore.

"The ore body is shallow having only 20 feet of over-burden. This means that it can easily be mined initially by the open-pit method * * *"

*Appendix —Opinion of the District Court*

*Stock Purchases and Stock Option Acquired by Fogarty*

The record establishes that prior to completion of the first test hole on November 12, 1963, Fogarty had purchased a total of 705 shares of TGS stock. On that date he purchased 300 shares, on November 15, 700 shares, on November 19, 500 shares and on November 26, an additional 200 shares. On December 30 and 31, 1963, which was about two weeks after the company received the chemical assay reports on the core taken from the first hole, Fogarty purchased 300 shares. Drilling was resumed on March 31, 1964, and the following day Fogarty bought 400 shares of TGS stock, and an additional 300 shares on April 6, making a total of 3100 shares of TGS stock purchased between November 12, 1963, and April 6, 1964.

On February 20, 1964, Fogarty received a stock option for 7300 shares of TGS stock. Other TGS officials also accepted stock options on that date. The evidence establishes that members of the stock option committee were not aware of the results of drilling near Timmins at the time the stock options were awarded. Fogarty subsequently surrendered his stock option unexercised, and "returned" to the company at his cost all stock purchased by him during the period November 12, 1963 to April 6, 1964. The record discloses that other TGS officials, including Richard D. Mollison, vice president in charge of exploration, and the company's chief geologist, Walter Holyk, either personally or through agents purchased TGS stock during the same period, as did several other employees of the company.[10] All purchases of TGS stock by Fogarty were made through the New York stock exchange.

10. Some of the purchases were of "calls" for TGS stock. A "call" is a negotiable option contract by which the bearer has the right to buy from the writer of the contract a certain number of shares of a particular stock at a fixed price on or before a certain agreed-upon date.

*Purchases and Sales of TGS Stock by Plaintiffs*

Plaintiffs purchased and sold stock in Texas Gulf Sulphur Company as follows:

*George Gordon Reynolds*: purchased 300 shares January 7, 1960, at $18⅝ per share, and 200 shares on May 18, 1962, at $15 per share. He sold 500 shares on April 16, 1964, at $33⅝ per share.

*Arthur R. Stout and wife*: purchased 1,000 shares February 5, 1962 for $20½ per share. They sold 1,000 shares April 21, 1964, at $42 per share.

*Lawrence L. Karlson and wife*: purchased 100 shares on October 10, 1963, for $16⅝ per share, and sold the same on December 11, 1963, for $20⅞ per share.

*Walter A. Mitchell*: purchased 420 shares between December 11, 1953, and May 17, 1962, at prices ranging from $15 to $80¼ per share. He sold 400 shares on April 17, 1964, for $40 per share, and 20 shares on April 23, 1964, for $46¼ per share.

VIOLATIONS OF SECTION 10(B) AND RULE 10B-5

Common to the complaints in all four cases are alleged violations of Section 10(b) of the Securities and Exchange Act of 1934,[11] and Securities and Exchange Commission Rule 10b-5.[12] The statutory provision in part provides:

"Sec. 78j. *Manipulative and deceptive devices.*

"It shall be unlawful for any person directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

* * *

11. 15 U.S.C. Section 78j(b).

12. 17 C.F.R. 240.10b-5.

"(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

The S.E.C. Rule, which is patterned in form and language after Section 17(a) of the Securities Act of 1933,[13] provides:

"It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person."

Neither the statute nor the Rule expressly provides for private civil remedies for fraud or misrepresentation in connection with a purchase or sale of any security, manipulative or deceptive practices, or for failing to disclose material information not otherwise available to the other

Reynolds, et al, vs. Texas Gulf Sulphur Company, et al

13. 15 U.S.C. 77q.

party to a transaction. Judicial decisions, however, have firmly established such civil remedies as being implicit in the provisions. A leading case, *Kardon* v. *National Gypsum Co.*[14] has been cited and followed in a number of later cases. In *Hooper* v. *Mountain States Securities Corp.*, the court said:

> "We need not repeat here the history now so well catalogued which traces the exercise by the SEC of the legislative power granted in Sec. 10(b) to promulgate regulation X-10B-5. A significant purpose of X-10B-5 was to extend to *sellers* the same protection against fraudulent and other unlawful schemes afforded to those defrauded in the purchase of securities. In a substantive way it is even more sweeping. It greatly expands the protection frequently so hemmed in by the traditional concepts of common law misrepresentation and deceit, the requirement of privity, proof of specific damage, inadequacy of the right of recission or right to recover up to par value of stock of a much greater market value. To these difficulties would have to be added the geographic obstacle of suit in a common forum against multi-state defendants scattered as far as the fraudulent device required * * *"

In the case of *Speed* v. *Transamerica Corp.*, supra, the court held that an implied misrepresentation can be just as fraudulent as an express one, that the three sub-paragraphs of Rule 10b-5 are mutually supporting and not mu-

14. 73 F.Supp. 798 (E.D. Pa. 1947). See also Fischman v. Ratheon Mfg. Co., 188 F.2d 783 (2d Cir. 1951); Speed v. Transamerica Corp., 99 F.Supp. 808; Hooper v. Mountain States Securities Corp., 282 F.2d 195 (5th Cir. 1960), cert. den. 365 U.S. 814 (1961); Slavin v. Germantown Fire Ins. Co., 174 F.2d 799 (3rd Cir. 1949); Fratt v. Robinson, 203 F.2d 627 (9th Cir. 1962); Stevens v. Vowell, 343 F.2d 374 (10th Cir. 1965); Kohler v. Kohler, 208 F.Supp. 808 (E.D. Wis. 1962), aff'd 319 F.2d 634 (7th Cir. 1963).

tually exclusive, and that a defendant's breach of duty to disclose accordingly can be viewed as a violation of all three sub-paragraphs, i.e., (1) a device, scheme, or artifice to defraud, (2) an implied misrepresentation or misleading omission, and (3) an act, practice or course of business which operates or would operate as a fraud.

Plaintiffs here contend that they have been damaged by violations of the statute and the rule by both the corporation and Fogarty, its executive vice president, (1) for failure to disclose prior to April 16, 1964, information as to the results of drilling at the property, and (2) in issuing an inaccurate, misleading and deceptive press release, which was published April 13, 1964. The decision to maintain secrecy and to not disclose the results of the drilling was made or concurred in by the president of the company, Claude O. Stephens, the executive vice president, Charles F. Fogarty, the vice president in charge of exploration, Richard D. Mollison, the company's chief geologist, Walter Holyk, and some other company officials and employees. Obviously, this was a decision of the corporation itself, even though some officers and directors were not informed of the drilling results until a public announcement was made on April 16, 1964.

*Karlson Case*

Plaintiff Karlson sold his stock on December 11, 1963, through a stock exchange. There was no face-to-face transaction. Fogarty did not purchase the particular shares sold by Karlson. While it is not necessary for Karlson to establish privity of contract in order to recover for violations of the statute or rule,[15] and the fact that there was a total non-disclosure would not prevent recovery if some

15. Cochran v. Channing Corp., 211 F.Supp. 239 (S.D. N.Y. 1962); Fischman v. Ratheon Mfg. Co., 188 F.2d 783 (2d Cir. 1951).

form of manipulation was involved,[16] it nevertheless is necessary for Karlson to prove some causative effect.

In the case brought against Texas Gulf Sulphur Company, Fogarty and other TGS officials and employees, by the Securities and Exchange Commission,[17] the Circuit Court found that Fogarty had violated Section 10(b) and Rule 10b-5 by purchasing TGS stock without publicly disclosing the insider information he possessed. It does not follow that such purchases by Fogarty, some of which were made prior to the time Karlson sold his stock, caused any damage to Karlson, and the record before us does not support any such contention. Corporations and their executives undoubtedly owe duties to stockholders to keep them reasonably informed as to corporate affairs and such matters as the mineral discovery here involved, but that duty does not surpass all other duties owed to stockholders. Here, for instance, the company and Fogarty were also under a duty to TGS stockholders, including Plaintiff Karlson, to not make information concerning the mineral discovery public until the company could first protect itself by acquiring mineral interests in adjoining lands. Plaintiff Karlson sold his TGS stock barely a month after completion of the first test hole and before the company had received all of the reports of the chemical analysis of the core extracted from that hole. The record discloses that such reports were received during the period December 9 to 13. He also sold prior to the time the company had been able to acquire the adjoining lands upon which the anomaly was found. The court believes it is not necessary to pass upon the materiality[18] of the information available to defendants on December 11, 1963, because of his findings

16. List v. Fashion Park, Inc., 340 F.2d 457 (2d Cir. 1965), cert. den. 382 U.S. 811 (1965).

17. Securities and Exchange Commission v. Texas Gulf Sulphur, et al., 401 F.2d 833, 842 (adv. sheets) (2d Cir. 1968).

18. See sub-paragraph (2) of Rule 10b-5, supra.

that there was no duty at that time on the part of either defendant to disclose the information then available with respect to drilling results, and that Fogarty's violations of the statute and the rule by purchasing TGS stock did not cause any damage to Plaintiff Karlson. The press release which the court has found to be misleading and inaccurate was not issued until four months after Karlson sold his stock.

*Reynolds Case*

Plaintiff Reynolds made two purchases of TGS stock, 300 shares on January 7, 1960, at $18⅝ a share, and 200 shares on May 18, 1962, at $15 per share. He sold his 500 shares early on the morning of April 16, 1964, after hearing about a "rumor" and a "flurry" in the stock, but before he learned that there had been an announcement of a "major strike" or "discovery." He testified that he sold on the strength of the April 12, 1964 press release, a summary of which came over the wires on the morning of April 13th.

An account executive with the Salt Lake City office of a national brokerage firm testified that after he read the summary of the April 12 release he telephoned Reynolds because he knew Reynolds was vitally concerned about TGS stock; that during their conversation he told Reynolds that the report "didn't make any positive statements about what had happened" and "that the report * * * didn't seem to substantiate the price action of the stock to that point." Reynolds testified that on the 13th he decided to hold the stock to see what happened, that he believed the press release, but that it made him feel that "someone was throwing a wet blanket" and that they were trying to say "we haven't got it."

Reynolds further testified that on April 16 the same account executive called him and "said there was a rumor

that Texas Gulf Sulphur had made a strike"; that he (Reynolds) "hardly believed it" but "thought it was a promotion propaganda of some kind" and decided to "get out while the getting was good." He sold his stock through the broker for $33⅝ per share. He also testified that if it hadn't been for the release which came over the wires on the 13th he would have kept his TGS stock; that if he had known of the November, 1963, test core hole he would have doubled his holdings. He did not learn of the contents of the April 16 release until later in the afternoon of that day (April 16) when the stock closed around $37, and that he did not buy back because "very few investors will ever chase a stock" and because he had already sold and was in a position where he would have to pay taxes on his profits.

From the record the court concludes that the press release dated April 12, 1964, was inaccurate, misleading and deceptive with respect to material matters disclosed by the company's drilling near Timmins. The authors of the release knew from visual and chemical analyses that the first core disclosed the presence of copper and zinc mineralization of ore-grade;[19] that the second test hole (K-55-3) virtually eliminated any chance that the initial test hole had been drilled "down-dip"; that cores from drill holes located 200 feet south and 200 feet north of the initial test hole contained similar mineralization; and that still another drill hole core had disclosed similar mineral-

19. In the Memorandum for the Files, previously referred to, prepared on November 14, 1963, by Chief Geologist Holyk, he wrote that the intersection encountered in the first drill hole was "obviously of ore grade." An article in the April 24, 1964 issue of the Wall Street Journal (part of defendant's Exhibit P-2) states that at the annual meeting of TGS stockholders held April 23, 1964 at Houston, the president of TGS in responding to questions from stockholders stated that "When we drilled the first hole, we knew we had something. But Canadian newspapers were carrying reports with no basis whatsoever."

ization at greater depths than were reached by the other drill holes.

The release painted a bleak and gloomy picture—most of the areas drilled in Eastern Canada revealed either barren pyrite or graphite without value; a few resulted in discoveries of small or marginal sulphide ore bodies, etc. Not a word, however, about the results of any of the drilling near Timmins, except that it had led to "preliminary indications" that more drilling would be necessary for a proper evaluation. The drilling "to date had not been conclusive" and has not been "sufficient to reach definite conclusions" and "any" statement "as to size and grade of ore would be premature and possibly misleading." But a newspaper reporter's finding, made on the same day the press release was printed, that the drillings indicated more than 10,000,000 tons of ore, and the same reporter's statement that one hole averaged in excess of 1% copper and 8% zinc, went unchallenged when submitted to vice president Richard D. Mollison who released the article on April 15th for publication. Obviously, the reporter was quoting figures given to him by officials of the company, and given to him on April 13th. It may very well have been that the company officials when they prepared the release dated April 12, were trying to hold the big news until just before, or on the day of, the Stockholders annual meeting which was held on April 23rd. In any event, the court finds the release dated April 12 was deceptive, misleading and inaccurate and violated both the statutory section 10(b) and the Rule provision 10b-5, and finds that plaintiff Reynolds was misled and deceived to his detriment, and is entitled to recover damages.

With respect to Mr. Ackerley's statement that from his examination on the 13th of April there were in excess of 10,000,000 tons of ore indicated, it is interesting to note the testimony of one of plaintiffs' witnesses, Dr. Francis

W. Christiansen, a geologist. Dr. Christiansen testified that from his examination of cores, assays, logs and other data pertaining to drilling up to 7:00 p.m. on April 10, he calculated the indicated tonnage of ore at 7,390,000 tons. He testified further that drilling up to 7:00 p.m. on April 11, added 2,600,000 tons of indicated ore, and that drilling up to the evening of April 12 added 1,800,000 tons more, making a total 11,790,000 tons of indicated ore as of Sunday evening, April 12th.

*Mitchell Case*

Plaintiff Mitchell, a C.P.A., residing in Los Angeles, purchased 420 shares of TGS stock between December 11, 1953 and May 17, 1962, at prices from $15 to $80¼ per share. On April 16, 1964, the first free day he had had following the income tax season, he stopped by to see one of his brokers between 9:00 and 9:30 a.m., to inquire about TGS stock which he had noticed had been rising over several weeks. His broker gave him a copy of the "New York Morning News Digest", dated April 13, 1964, published by E. F. Hutton & Company, in which appeared the following:

> "In the financial press this morning, management of Texas Gulf Sulphur states that reports that it has discovered a large lode of rich copper in Canada are premature and possibly misleading."

He also read the article in the western edition of the Wall Street Journal for April 13, 1964, the first paragraph of which read:

> "New York—Texas Gulf Sulphur Co. called reports that it has discovered a large lode of rich copper ore in Canada 'premature and possibly misleading.' "

After reading the foregoing articles Mr. Mitchell returned to his office, reviewed his file on TGS and "came to the conclusion, based upon the report, the release of April

13 by Texas Gulf Sulphur, that the stock could not sustain its present rise and that it would fall back as soon as that release had been disseminated and recognition given to it by the public." He then went to a second broker and instructed him to sell 400 shares. It was a "short sale against the box." This was about 11:30 or 11:45 a.m. Later in the afternoon he discovered he had overlooked 20 shares and when he took the certificates for the 400 shares in to his broker he told the clerk that he would bring in the 20 shares the following morning and that they were to be sold. They were delivered on the morning of the 17th with instructions to sell short against the box.

At the time Mitchell sold his stock he had no knowledge of any press release other than that of April 12th. Under cross-examination he testified that "the reason I sold short was that I did not want to part with my Texas Gulf Sulphur stock. I reasoned that inasmuch as the market could not sustain itself in view of the report—the release of April 13—that I could sell short, buy back at a lower price, and in the meantime retain the stock I owned; namely, the 420 shares * * *"[20] On the 16th the bid price was in the neighborhood of $37 so he sold 400 shares at $40 a share. When he took the 20 shares in on the 17th the stock had gone up somewhat and he put those shares in at $45. Even though he gave his broker instructions to sell the 20 shares on the 17th, for some reason unknown to plaintiff Mitchell, the

20. A "short sale" is defined as follows in Patton's Accountant's Handbook (3rd Ed.): "A short sale is a transaction in which a trader in securities 'sells' a block of stock at the current price without making immediate delivery. Such a sale is made in anticipation of a decline in the price of the security; the trader expects to make a profit by buying the stock—'covering'—at a lower price. The postponing of delivery by the vendor is made possible through an arrangement by which the broker 'borrows' the stock for delivery to the party to whom the sale was made. Under the usual plan the trader is not required to cover as long as his account with the broker is properly protected."

order to sell was not put through by the broker until April 22, and the stock was sold on the 23rd for $46¼ per share.

Plaintiff Mitchell testified that the article in the Wall Street Journal of April 13 "was the motivation that caused me to sell short."

The court agrees with Plaintiff Mitchell that the press release dated April 12, 1964, was false, misleading, deceptive and fraudulent; that it contained misstatements of material facts and omitted and concealed material facts with respect to the progress of drilling—all in violation of Section 10(b) of the Securities Exchange Act of 1934, and S.E.C. Rule 10b-5. It omitted all information as to the results of chemical and visual appraisals of cores, and gave no information as to the number of holes drilled or the type of mineralization encountered. It was a misstatement to say that recent drilling had led to "preliminary indications that more drilling would be required for proper evaluations of this prospect" and it was deceptive to state that "work done to date has not been sufficient to reach definite conclusions and *any* statement as to size and grade of ore would be premature and possibly misleading" (emphasis added). The tenor of the entire statement was misleading, and, the court thinks designedly so.

*Stout Case*

Arthur R. Stout, Jr. and his wife owned 1,000 shares of TGS stock in joint tenancy, which had been purchased on February 5, 1962, at $21½ a share. Their order to sell was placed April 21, 1964, and the stock was sold the following day at $42 per share. Mr. Stout testified that the sale of the stock was motivated by information concerning the press release of April 12, 1964, which he received "probably within a week of the 13th." He had no recollection as to how he received the information, but from what he heard he "concluded that the officers of Texas Gulf

Sulphur had stated that the discovery was overrated and exaggerated and that, as a result of their statements, the stock would (go down) in price, and therefore I sold it." Mr. Stout testified that he had bought TGS stock for long-term appreciation; that he had no need for money when he sold it; and that the money received from the sale he put into a bank savings account. He stated: "I received that information. Whether I read it or heard it through the news media, I do not recall; but the essence of the information of the release is what I based the sale of my stock on."

One of the allegations in the Stout complaint is the following:

> "Confused by conflicting reports issued by defendants of the value of the Kidd 55 segment, plaintiffs sold their 1,000 shares on or about April 22, 1964, at a price of $42.00 per share."

The Stouts ask for rescission, or, in the alternative, damages, contending that the actions of defendants in preparing, issuing and causing the news release dated April 12, 1964, to be published were fraudulent; that the release misstated or concealed the true facts concerning the magnitude of the mineral discovery; that defendants knew the facts given were incorrect and misleading and knew, or should have known, that the facts as stated would be relied upon by shareholders. The court thinks these statements constitute a fair appraisal of the nature, purpose and effect of the April 12, 1964, news release.

DAMAGES

It is unnecessary for the court to make any determination as to whether defendants were required by the statute or the rule to disclose the results of drilling at any time prior to April 12, 1964. Likewise, nothing would be gained by exploring the question whether the wide-spread rumors

in Canada and in this country gave rise to a duty on the part of the defendants to make a disclosure prior to that date.

The important fact is that defendants chose to issue a public statement, which both the statute and the rule required be accurate, fair and complete. Instead, the press release issued by defendants was misleading, intentionally deceptive, inaccurate and knowingly deficient in material facts pertaining to the results of drilling. The record establishes that each of the plaintiffs relied upon the misleading and inaccurate announcement in making his decision to sell his TGS stock. Consequently, defendant Texas Gulf Sulphur must respond in damages.

The aim of courts in cases of this type is to put the plaintiffs in the positions they would have been in if they had not been motivated by defendants' fraudulent press release to sell their stock. In this connection it is significant to point to the periods of time plaintiffs had held their stock. Plaintiff Reynolds, when he sold 500 shares of TGS stock on April 16, 1964, had held 300 shares since January 7, 1960, a period of more than four years, and had held 200 shares since May 18, 1962, a period of 23 months. Plaintiffs Stout sold 1000 shares of TGS stock on April 21, 1964. They had held those shares since February 5, 1962, more than two years. Plaintiff Mitchell purchased 420 shares of TGS stock at various times during the period December 11, 1953 and May 17, 1962. Some of the 400 shares he sold on April 17, 1964, he had held for more than 10 years, some about two years.

The variety of situations in which a 10(b) or 10b-5 violation may be found makes it difficult to formulate a comprehensive rule of damages. In the case of *J.I. Case Company* v. *Borak*, 377 U.S. 426, where violations of the Securities Exchange Act were involved, the Supreme Court observed that it is the duty of the courts to be alert to

provide such remedies as are necessary to make effective the congressional purpose, that where federally secured rights are invaded federal courts should adjust their remedies so as to grant necessary relief, and that they may use any available remedy to make good the wrong done.

Section 28(a) of the Securities Exchange Act[21] provides that "no person permitted to maintain a suit for damages under the provisions of this title shall recover * * * a total amount in excess of his actual damages * * *", but it provides no help in determining how "actual damages" are to be measured.

It seems to this court that the true and just measure of damages in these cases should be, with some qualification, what long ago came to be called the New York Rule. Of necessity, it was unthinkable that the common law rule in trover for the conversion of ordinary chattels, i.e., fair market value at time of conversion, should be applied in the case of corporate shares with rapidly changing values. So the rule evolved that the measure of damages in stock transactions is the highest intermediate value reached by the stock between the time of the wrongful act complained of and a reasonable time after the injured party received, or should have received notice of it, a time within which he has a reasonable opportunity to replace the stock. This was announced by the United States Supreme Court in a case decided in 1888 which arose in the Territory of Utah, *Galigher* v. *Jones*, 129 U.S. 194, 200-202.[22]

Factors considered in making the judgment on damages in this case include: the rapidity of price fluctuations in normal trading situations on the New York market; the excessive publicity, first having a tendency to depress the

21. 15 U.S.C. Sec. 78bb(a).

22. The former rule of highest intermediate value up to time of trial was repudiated.

price of Texas Gulf Sulphur shares, and later to cause it to rise, the nature of the Texas Gulf Sulphur enterprise; that is, a mining venture carrying on world wide mineral explorations, about which there has been extensive continuing publicity, all of which reasonably might have been expected to cause stockholders' interest to be stimulated and to cause them to be on the alert for sudden changes in the quotations, and to exercise ordinary care, prudence, and diligence in watching out for their own interest, and to learn of the Texas Gulf Sulphur announcement of April 16.

The obligation of the plaintiff shareholder is to exercise ordinary and reasonable care and diligence to look out for himself. The notice required is that which he received, or should have received, in the exercise of reasonable care and diligence.

We must draw the line somewhere, and this is an attempt to give a twenty trading day period within which the average of the highest daily prices is the measure of damages, and a period within which the shareholders received, or should have received, notice of the Texas Gulf Sulphur announcement of April 16.

A few days, is too short a time reasonably to expect stockholders to make a judgment and sell their stock, and much too early to let the New York market reflect the true value, over-stimulated upward or downward. The average of the highest daily sales for the 16th of April and 19 trading days subsequent thereto allows the market reactions more truly to reflect actual value and allows a more reasonable period of time within which to require the shareholders, in the exercise of ordinary diligence and prudence, to learn of the Texas Gulf Sulphur announcement of April 16 and to protect their interest.

There remain a couple of additional factors considered by the court in reaching the judgment in this case. They were suggested in Judge Henry J. Friendly's opinion in the

Second Circuit, *Securities and Exchange Commission* v. *Texas Gulf Sulphur*, 401 F.2d 864, 866-867.

Judge Friendly was speaking of "negligence" in the drafting of the release. Instead, the record here discloses that the press release issued by defendants was misleading, intentionally deceptive, inaccurate and knowingly deficient in material facts.

One of the choices open to the corporation, if it decides to speak, is to tell the truth.

The measure of damages here adopted is calculated to result in fair, reasonable and just awards. The damages awarded are compensatory and not punitive or *in terrorem*. Plaintiffs are only to be made whole, not to be compensated twice. When plaintiffs recover compensation for their losses from Texas Gulf Sulphur their claims against Fogarty will be deemed paid, satisfied and discharged.

On the day, April 16, 1964, that TGS publicly acknowledged that it had made a substantial mineral discovery, its stock advanced nearly $7 to a high of $37. The following day it advanced to a high of $42, and on the next trading day it advanced to a high of $44. This was followed by a decline to a high of $41¼, then an increase of more than 5 points to a high of $47. On April 29, 1964, it reached a high of $59. After a number of declines and a few advances it reached $60.50 on May 18; 1964. The extent to which the stock fluctuated on each trading day, and from day to day, is apparent from the table set out in the footnote.[23]

---

23. The opening, high, low and closing prices of TGS stock for 20 trading days starting with April 16, 1964, are as follows:

| | | *Open* | *High* | *Low* | *Close* |
|---|---|---|---|---|---|
| April 16, 1964 | (Thurs.) | 30–⅛ | 37 | 30–⅛ | 36–⅜ |
| April 17, 1964 | (Fri.) | 39–¾ | 42 | 38–¾ | 40–¼ |
| April 20, 1964 | (Mon.) | 42 | 44 | 41–½ | 42–¼ |
| April 21, 1964 | (Tues.) | 41 | 41–¼ | 39–⅛ | 40–⅛ |
| April 22, 1964 | (Wed.) | 40–½ | 47 | 40–½ | 45–½ |

[*footnote continued on next page*]

In Section 151 of the Restatement of Restitution it is recognized that while generally the measure of recovery will be the value of the property at the time of its improper acquisition, retention or disposition, a "higher value" may be recognized "if this is required to avoid injustice where the property has fluctuated in value or additions have been made to it." Comment c. to Section 151 explains:

> "Where the subject matter is of fluctuating value, and where the persons deprived of it might have secured a higher amount for it had he not been so deprived, justice to him may require that the measure of recovery be more than the value at the time of deprivation. This is true where the recipient knowingly deprived the owner of his property or where a fiduciary in violation of his duty used the property of the beneficiary for his own benefit. In such cases the person deprived is entitled to be put in substantially the position in which he would have been had there not been the deprivation, and this may result in granting to him an amount equal to the highest value reached by the subject matter within a reasonable time after

[*footnote continued from preceding page*]

| | | *Open* | *High* | *Low* | *Close* |
|---|---|---|---|---|---|
| April 23, 1964 | (Thurs.) | 47–¾ | 48–¼ | 42–⅛ | 42–⅝ |
| April 24, 1964 | (Fri.) | 44 | 44–¾ | 42–¾ | 44–¼ |
| April 27, 1964 | (Mon.) | 44–⅞ | 47–½ | 44–⅝ | 47 |
| April 28, 1964 | (Tues.) | 47–¾ | 52–⅜ | 47–¾ | 52–⅜ |
| April 29, 1964 | (Wed.) | 54–½ | 59 | 53–½ | 56–¾ |
| April 30, 1964 | (Thurs.) | 54–½ | 58–⅜ | 54–½ | 54–¾ |
| May 1, 1964 | (Fri.) | 55–¾ | 56–⅞ | 52–½ | 52–⅞ |
| May 4, 1964 | (Mon.) | 54–½ | 54–⅝ | 52–⅛ | 52–⅝ |
| May 5, 1964 | (Tues.) | 51–¾ | 52 | 48–⅜ | 48–⅜ |
| May 6, 1964 | (Wed.) | 48–¼ | 52–¼ | 46–⅜ | 52–¼ |
| May 7, 1964 | (Thurs.) | 52–½ | 53–⅜ | 49–½ | 49–½ |
| May 8, 1964 | (Fri.) | 51–½ | 54–½ | 50–¼ | 54–⅛ |
| May 11, 1964 | (Mon.) | 54–⅞ | 57 | 54–⅝ | 56 |
| May 12, 1964 | (Tues.) | 55–⅞ | 56–⅜ | 53–½ | 55 |
| May 13, 1964 | (Wed.) | 54–¼ | 55–⅞ | 51–⅝ | 51–⅝ |

the tortious conduct. This is done if he can prove that he probably would have made a sale while the subject matter was at its highest point in value * * *"

In the wrongful conversion case of *Nephi Processing Plant* v. *Talbot*, 247 F.2d 771 (10th Cir. 1957) the Circuit Court held that while Utah courts have recognized that as a general rule the measure of damage for conversion of property is the value of the property at the time of conversion "the rule has no application where the converted chattels are of a kind which have a fluctuating market value." In such cases, the court said, "the measure of damages is the highest market price of the property within a reasonable time after the owner has notice of the conversion."

What a "reasonable time" may be will vary from case to case. Here, a period of wide-spread rumors about a mineral discovery was followed by the deceptive and inaccurate press release published April 13, 1964, and the public announcement of a major discovery on April 16, 1964. On that day the price of TGS stock jumped about $7, and for the next 9 trading days the stock steadily increased, except for two days on each of which the closing price of the stock decreased about $2. On the 10th trading day (including the day of the announcement) the stock had advanced from approximately $30 to a high of $59. During the ensuing 11 days the stock fluctuated considerably and then climbed to a new high for this period of $60.50 on May 18, 1964.

In the circumstances of these cases the court considers that a reasonable period would be 20 trading days including April 16, 1964, the day of the announcement.

If the plaintiffs had not been led to sell their TGS shares and learned on April 16th, through the TGS announcement, of the proportions of the discovery, it would

be highly improbable, to say the least, that any one of them would have sold at the highest price.

The court deems it fair and just therefore, to take the average of all of the highest market prices on the 20 trading days, rather than the single highest market price during the period.

The average of the high market prices during such 20-day period is $50.75, which the court adopts as the measure of damages in these cases.

Damages to be awarded to plaintiff Reynolds are computed by deducting from $50.75 the price he received for each share, $33.625, and multiplying the resulting figure of $17,125 by 500, the number of shares he sold, to arrive at damages of $8,562.25. Interest on that amount at the rate of 6% per annum from the date he sold his stock to the date of judgment is allowed.

Similarly, damages for Plaintiff Mitchell are computed by deduction from $50.75 the amount received by him for each share and multiplying the resulting figure by the number of shares to arrive at damages of $4,390.00. In the case of Plaintiffs Stout, damages are awarded in the sum of $8,750.00, arrived at in the same manner. In each case interest is awarded at the rate of 6% per annum on the damages from the date on which the TGS shares of stock were sold to the date of judgment.

The court does not overlook the claims of the Stouts that (1) they did not learn of the "possibility" of an action against defendants until "on or after July 12, 1966" and (2) that they "did not become aware of or learn of the defendants' unlawful actions in connection with the issuance of the April 12, 1964, press release until on or about July 12, 1966." Aside from doubts the court has as to the credibility of these claims, he believes that in the circumstances of this case the Stouts knew, or should have known, of the misrepresentations and deceptions in the April 12, 1964, release within a period of 20 trading days.

STATUTE OF LIMITATIONS

There is no federal statute of limitations which is applicable to violations of Section 10(b) of the Act or of Rule 10b-5, consequently the Utah statute of limitations, 78-12-26(3) Utah Code Annotated, 1953, controls. It provides:

> "Within three years: * * *
>
> "(3) An action for relief on the ground of fraud or mistake; but the cause of action in such case shall not be deemed to have accrued until the discovery by the aggrieved party of the facts constituting the fraud or mistake * * *"

The action brought by Plaintiff Reynolds was filed July 12, 1966, and the action brought by Plaintiffs Stout was filed April 7, 1967. Each of these actions was clearly within the statutory period.

The action commenced by Plaintiff Mitchell was filed April 17, 1967. Defendants contend this action should be dismissed as having been filed too late. Mitchell, a C.P.A., testified at the trial that on April 16, 1964, the first free day after the close of the income tax season, he visited one of his brokers and for the first time learned of the press release of April 12, 1964. He went back to his office, obtained the certificate for 400 shares of TGS stock and took it to another broker and gave him an order to sell. At that time he realized he had an additional 20 shares and he told the broker he would bring them in the next day, which he did and gave the order to sell the 20 shares on April 17. He testified that at the time he gave the orders to sell he knew of no press release from TGS other than that of April 12, 1964. In a deposition taken by defendants, Mitchell testified in response to questions as follows:

> "Q. Do you recall any conversation with Mr. Lewis with respect to your Texas Gulf Sulphur stock after

the conversation on the 16th at approximately 1:00 o'clock or 1:30 that you have just described to us?

"A. You mean that same week?

"Q. Yes, any time.

"A. Yes, I believe it was Wednesday or Thursday of the following week that I think Mr. Singer told me —I am not too sure—or did I read it in the Wall Street Journal something to the effect that a new release had come out on the 16th."

The Court has examined and considered the testimony of Mr. Mitchell and the rather extensive depositions taken by defendants of Mitchell and his brokers, and has concluded that the above quoted testimony should be accepted. Consequently, Mitchell's action was filed within the time limit set by the Utah statute.

Dated this 9th day of January, 1970.

/s/ Willis W. Ritter
WILLIS W. RITTER, CHIEF JUDGE

Filed: January 13, 1970

C-132-66

GEORGE GORDON REYNOLDS,

*Plaintiff,*

*v.*

TEXAS GULF SULPHUR COMPANY, a Texas Corporation, and CHARLES F. FOGARTY,

*Defendants.*

This is the third time plaintiff Reynolds has sought an order that this case may be maintained as a class action.

His first motion was denied after full hearing on February 2, 1967, and on February 6 a formal order was entered pursuant to Rule 23(d)(4) denying the motion and directing "that portion of plaintiff's complaint averring the existence of a proper class action is hereby dismissed with prejudice." Pertinent portions of that Order read:

> "1. That plaintiff failed to sustain the burden of producing facts which would justify a determination by the court that the above entitled action is a proper class action as required by Rule 23 of the Federal Rules of Civil Procedure, as amended.
>
> "2. That numerous actions involving similar issues of fact and law have heretofore been filed and are now pending before the United States District Court in the Southern District of New York, 32 of which actions purport to be class actions.

"3. That all of said actions on file in the Southern District of New York have been assigned to a single judge for discovery and for trial.

"4. That in addition to private actions on file in the United States District Court for the Southern District of New York, there is also pending a suit brought by the Securities and Exchange Commission against the defendants in this action and others arising from the same conduct on the part of defendants and involving similar issues of fact and law as are present in the various private actions; that said action by the SEC has been tried and that the trial court ruled that such conduct of the defendants did not violate the provisions of Section 10(b) of the Securities Exchange Act of 1934 or of Rule 10b-5 promulgated pursuant thereto; that said action by the SEC is now pending on appeal before the United States Court of Appeals for the Second Circuit and has been set for hearing for oral argument in the month of March, 1967; and that the various private actions now pending in the State of New York are being held in abeyance voluntarily by the respective parties pending the decision of the Court of Appeals in the SEC case.

"5. That a determination that this action is a proper class action would unduly complicate the pending litigation described above.

"6. That if the various private suits are to be concentrated for trial in a single forum, they should be concentrated in the Southern District of New York and not in this District.

"7. That substantial difficulties would be encountered in attempting to manage the proposed class action from this District.

"8. That discovery sufficient to identify members of the proposed class would be extremely time-consuming and expensive. The number of such members appears to

be in the thousands, most of whom reside in the East and few, if indeed any, other than plaintiff in Utah."

The propriety of a class action was considered a second time on September 29, 1967 when this court granted defendants' motion to dismiss the class action allegations in the consolidated cases, and on October 12, 1967 a second order was entered "That all averments and references to class actions in the complaints of the consolidated cases be and the same are hereby stricken." At no time thereafter prior to trial or prior to this court's decision on the merits did plaintiffs seek to reargue or renew their motions nor seek leave to appeal this court's determinations on the point. The action proceeded solely on the basis that it was to determine the rights of the named plaintiffs, and their rights alone.

For the third time, and at this late date, and in the form of a "Motion for the Entry of Additional Findings of Fact and Conclusions of Law Concerning Class Action", plaintiff Reynolds "prays that a time be set for the further hearing of counsel with respect to the question of the class action proceedings • • • the court vacate its order of October 12, 1967, striking the allegations of a class action, order that this action be maintained as a class action and enter findings of fact and conclusions of law with respect thereto in the form attached hereto."

Plaintiff Reynolds seeks to represent the class of all sellers from April 13 to April 16, both inclusive. On April 13, 1964, there were 126,500 shares of Texas Gulf stock sold on the New York Stock Exchange; on April 14, there were 76,900 shares sold; on April 15, there were 43,800 shares sold; on April 16, there were 444,200 shares sold; the total shares sold on these four dates is 691,400. There would necessarily be several thousand members of the alleged class. Each of those persons would

eventually have to be deposed, produce documents and prove his individual case on causation, reliance and damages. There can be no question but that there were differences in the kinds and degrees of reliance by the persons to whom the April 12 release was addressed, as demonstrated by plaintiffs Reynolds, Mitchell and Stout. There were material variations in the manner in which the April 12 press release was conveyed to the investing public.

Pre-trial discovery and actual testimony would be necessary before there could be recovery.

In my judgment, as I have said before, if these various private suits are to be concentrated for trial in a single forum they should be concentrated in the Southern District of New York and not in this District. Among other reasons, an important one is that the bulk of this litigation is already there.

The Securiies and Exchange Commission had commenced in New York its suit in equity against Texas Gulf Sulphur on April 19, 1965, more than a year before the Reynolds suit was instituted. Judge Dudley Bonsal decided the case against the Commission in August of 1965. The Commission appealed and the Second Circuit determined to hear it *en banc*.

The decision of the Second Circuit came down August 3, 1968, reversing the District Court. The Second Circuit did not determine that Texas Gulf's April 12 press release violated the securities laws. Rather it remanded:

> "Accordingly, we remand this isue to the district court that took testimony and heard and saw the witnesses for a determination of the character of the release in the light of the facts existing at the time of the release, by applying the standard of whether the reasonable investor, in the exercise of due care, would have been misled by it." (401 F.2d 833, 863).

If this question were resolved against Texas Gulf, the District Court would be required on remand then to determine whether the release was issued as a result of "a lack of due diligence" on the part of Texas Gulf. The trial of these issues was held before Judge Bonsal on October 6, 7 and 8, 1969. The opinion has not yet come down.

The Second Circuit has indicated some guide lines to the New York District Court.

On October 22, 1969, in addition to the SEC suit, 94 other actions had been brought in New York against Texas Gulf and individual defendants. All told there were more than 500 named plaintiffs seeking damages in the sale of 150,000 shares of Texas Gulf stock during the period November 12, 1963 through April 16, 1964. Named plaintiffs in the case then pending before Judge Bonsal who sold in the period April 13 through April 16, both inclusive, claim damages on sales of approximately 29,000 shares of Texas Gulf stock. (Affidavit of Orison S. Marden, filed October 27, 1969).

In two actions in the Southern District of New York Judge Bonsal, on March 20, 1969, ruled that the cases might proceed as class actions. These cases are *Cannon* v. *Texas Gulf* and *Green* v. *Texas Gulf*, 47 F.R.D. 60 (S.D. N.Y. 1969).

In the *Cannon* action 20 named plaintiffs claimed damages on sales of 4,020 shares of Texas Gulf stock during the period April 12, 1964 through April 16, 1964, and in the companion action of *Green* v. *Texas Gulf Sulphur Co.*, 26 plaintiffs claimed to have sold a total of 4,453 shares of Texas Gulf Sulphur Company stock during that period in reliance upon the Company's April 12 press release. At the October 30, 1968 hearing on the motion for class action, attorneys for plaintiffs in some 59

actions had the opportunity to be heard. (Affidavit of Orison S. Marsden).

Following Judge Bonsal's ruling in the *Cannon* & *Green* cases, the attorneys began the necessary steps to identify the members of the class they claimed to represnt. Discovery procedures commenced April 15, 1969 revealed that Texas Gulf did not have any records which could identify the class.

Thereafter, plaintiffs' attorneys began the tedious and time consuming procedure of identifying potential plaintiffs described in the Marden affidavit:

> "They deposed the Stock Clearing Corporation in New York on May 2, 1969. The Stock Clearing Corporation produced the Daily Reconciliation Lists for cleared trades in the common stock of Texas Gulf Sulphur Company for the dates of April 13, 14, 15 and 16, 1964. These records, compiled from the trade information submitted by the various Purchase and Sales Departments of the clearing member organizations, matches [sic] the purchasing broker's records. This information is then reproduced by computer to allow the clearing members to affect [sic] deliveries of Texas Gulf stock.
>
> "The records of the Stock Clearing Corporation which were produced consisted of 69 computer print-out sheets which recorded the transactions on those four trading days. In code it lists the selling broker, the purchasing broker, the number of shares in each transaction, the price per share and total price of the trade.
>
> Approximately 3900 separate transactions are recorded, all transactions involving lots of 100 shares or more.
>
> "The next step in attempting to find and identify the sellers of stock during this period is to depose or otherwise obtain the necesary identifying information from the various clearing brokerage houses, of which there are more

than 225, in order to discover for whom each brokerage house was acting. Of course, many of the transactions are sales by the odd-lot houses, acting as agents for several different persons as to each 100 share sale. The Stock Clearing Corporation produced the code for the brokerage houses. We have not ascertained how many of these were involved in transactions in Texas Gulf stock, but they are numerous. We do not know what steps have yet been undertaken by counsel for plaintiffs in *Cannon* and *Green* in this direction, but it is likely that this has not begun. It is the necessary next step in order to determine who the members of the class are, but we believe they have not gone ahead because of pending motions by defendants for summary judgment, raising questions of law which have not yet been passed upon by Judge Bonsal."

The pending motions in 60 actions for summary judgment referred to by Mr. Marden in his affidavit sworn to on October 22, 1969, and filed here October 27, were ruled on by Judge Bonsal October 31, 1969. *Astor, et al.* v. *Texas Gulf Sulphur Co., et al; Alexander, et al.* v. *Texas Gulf Sulphur Co., et al; Darraugh, Jr., et al.* v. *Coates, et al.* (CCH Fed. Sec. L. Rep. paragraph 92, 501)

A hearing was held in the *Cannon* and *Green* cases on December 8, 1969, at which time Judge Bonsal directed counsel to settle an order to obtain information from the brokers referred to above by Mr. Marden as to who are the members of the class, and Judge Bonsal considered the kind of notice to be sent out to the members of the class.

In reaching a judgment upon this motion, the foregoing facts have been considered with Rule 23(b) (B) (3) in mind, particularly clauses: (B) The extent and nature of any litigation already commenced by members of the class. (C) The desirability or undesirability of concentrating the litigation in the

particular forum. (D) The difficulties likely to be encountered in the management of a class action in Salt Lake City.

The application of these provisions of Rule 23 to the facts and circumstances herein outlined seem to the Court particularly appropriate. The litigation in New York is far advanced, far and away the bulk of the cases are there, and the information necessarily to be obtained from the brokerage offices is more readily and more conveniently available in New York City.

Dated this 13th day of January, 1970.

/s/ Willis W. Ritter
Willis W. Ritter, Chief Judge

Filed: January 13, 1970

## Judgments of the District Court (Entered January 13, 1970)

UNITED STATES DISTRICT COURT

DISTRICT OF UTAH, CENTRAL DIVISION

C-62-67

WALTER A. MITCHELL,

*Plaintiff,*

*v.*

TEXAS GULF SULPHUR COMPANY, a Texas Corporation, and CHARLES F. FOGARTY,

*Defendants.*

The above-captioned matter was consolidated for trial with three other cases, George Gordon Reynolds v. Texas Gulf Sulphur Company, et al. (Civil No. C-132-66), Arthur R. Stout, et al. v. Texas Gulf Sulphur Company, et al., and Lawrence L. Karlson et al. v. Texas Gulf Sulphur Company, et al. (Civil No. C-59-67), and the consolidated matter was tried to the Court, sitting without a jury, the Honorable Willis W. Ritter, Chief Judge, presiding, the plaintiff Walter A. Mitchell being represented by Roy G. Haslam, Esq., and the defendants Texas Gulf Sulphur Company and Charles F. Fogarty being represented by Calvin A. Behle, Esq., Keith E. Taylor, Esq., Orison S. Marden, Esq., and P. B. Konrad Knake, Esq., and the Court having received

certain stipulations of fact entered into by the parties and having received evidence, both testimonial and documentary; and having heard the arguments of counsel and being fully advised in the premises, and having filed its Amended Findings of Fact and Conclusion of Law:

IT IS HEREBY ORDERED, ADJUDGED AND DECREED:

That plaintiff be awarded judgment against defendants in the sum of $4,390.00, together with interest thereon at the rate of six per cent (6%) per annum to the date of judgment herein, and costs incurred in the maintenance of this action. Interest shall be calculated from April 16, 1964, to the date of judgment herein on that portion of the total damages incurred through the sale of 400 shares of Texas Gulf Sulphur Company stock, and from April 23, 1964 to the date of judgment herein on that portion of the total damages incurred through the sale of 20 shares of Texas Gulf Sulphur Company stock.

Dated this 13th day of January, 1970.

/s/ Willis W. Ritter
WILLIS W. RITTER, CHIEF JUDGE

Entered: January 13, 1970

**C-132-66**

GEORGE GORDON REYNOLDS,

*Plaintiff,*

*v.*

TEXAS GULF SULPHUR COMPANY, a Texas Corporation, and CHARLES F. FOGARTY,

*Defendants.*

The above captioned matter was consolidated for trial with the cases of Walter A. Mitchell v. Texas Gulf Sulphur Company, et al. (Civil No. C-62-67), Lawrence L. Karlson, et al. v. Texas Gulf Sulphur Company, et al. (Civil No. C-59-67), and Arthur R. Stout et al. v. Texas Gulf Sulphur Company et al. (Civil No. C-54-67), and the consolidated matter was tried to the Court, sitting without a jury, the Honorable Willis W. Ritter, Chief Judge, presiding, the plaintiff George Gordon Reynolds being represented by Parker M. Nielson, Esq., and A. Reed Reynolds, Esq., and the defendants Charles F. Fogarty and Texas Gulf Sulphur Company being represented by Calvin A. Behle, Esq., Keith E. Taylor, Esq., Orison S. Marden, Esq., and P. B. Konrad Knake, Esq., and the Court having received certain stipulations of fact entered into by the parties and having received evidence, both testimonial and documentary, and having heard the arguments of counsel and being fully advised in the premises and having made and filed its Amended Findings of Fact and Conclusions of Law herein:

NOW, THEREFORE, it is hereby ORDERED, ADJUDGED AND DECREED:

That Plaintiff George Gordon Reynolds is granted judgment against the defendants in the amount of $8,562.50, together with interest thereon at the rate of six per cent (6%) per annum from April 16, 1964, to the date of entry of judgment herein, and costs incurred in the maintenance of this action.

Dated this 13th day of January, 1970.

/s/ Willis W. Ritter
WILLIS W. RITTER, CHIEF JUDGE

Entered: January 13, 1970

C-132-66

GEORGE GORDON REYNOLDS,

*Plaintiff,*

*v.*

TEXAS GULF SULPHUR COMPANY, a Texas Corporation, and CHARLES F. FOGARTY,

*Defendants.*

The Court, having heard oral arguments of counsel for the parties and of counsel for persons appearing *amicus curiae*, on two occasions, relative to plaintiff's Motion for the Entry of Additional Findings of Fact and Conclusions of Law Concerning Class Action, and having read and considered memoranda supplied by all parties and persons concerned, and being fully advised in the premises, upon the grounds and for the reasons set forth at some length in the following Memorandum,

IT IS ORDERED, that the motion be, and the same hereby is denied.

DATED this 13th day of January, 1970.

Willis W. Ritter, Chief Judge
/s/ Willis W. Ritter

Filed: January 13, 1970

## Opinion of the Court of Appeals
## (Decided April 26, 1971)

UNITED STATES DISTRICT COURT

TENTH CIRCUIT

MARCH, 1971, TERM

**Nos. 280-70**
**281-70**

WALTER A. MITCHELL,
*Appellee and Cross-Appellant,*

*v.*

TEXAS GULF SULPHUR COMPANY, *et al.*,
*Appellant and Cross-Appellee.*

---

**Nos. 282-70**
**283-70**

GEORGE GORDON REYNOLDS,
*Appellee and Cross-Appellant,*

*v.*

TEXAS GULF SULPHUR COMPANY, *et al.*,
*Appellant and Cross-Appellee.*

---

**Nos. 284-70**
**285-70**

ARTHUR R. STOUT, *et al.*,
*Appellees and Cross-Appellants,*

*v.*

TEXAS GULF SULPHUR COMPANY, *et al.*,
*Appellant and Cross-Appellee.*

---

**Appeal from the United States District Court for the District of Utah, Central Division**

Before LEWIS, Chief Judge, HILL and McWILLIAMS, United States Circuit Judges.

HILL, Circuit Judge.

Appellees and cross-appellants Reynolds, Mitchell and Stout instituted actions in the Utah district against appellants and cross-appellees Texas Gulf Sulphur Company (hereinafter referred to as TGS) and Charles A. Fogarty, one of the principal officers of the company, to recover damages for violations of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b) and Rule 10b-5, 17 C.F.R. §240.10b-5, promulgated thereunder. The actions were consolidated for trial to the court without a jury and plaintiffs procured judgments in the three cases.[1]

While the complaints of the several parties make varying allegations of legal infractions,[2] the cases were tried, and are appealed, only upon alleged violations of Section 10(b) and Rule 10b-5, with a cross-appeal by Reynolds and Mitchell on the issues of damages and class action claims. Specifically, the claim is that appellees were damaged by the violations of TGS and Fogarty, its executive vice president, (1) for failure to disclose on April 12 and prior to April 16, 1964, information as to the results of drilling at the Timmins property; and (2) in issuing an inaccurate, misleading and deceptive press release published April 13, 1964.

The essential facts are as follows: Reynolds, Mitchell and Stout were and had been for several years stockholders in TGS. After several years of extensive mineral exploration on the Canadian Shield of eastern Canada, TGS de-

1. The trial court's opinion, including findings and conclusions, is reported in 309 F.Supp. 548.

2. One complaint included a count in common law fraud, another alleged a conspiracy to violate the Act and Rule, and one alleged violation of fiduciary duties and violations of Section 9 of the Act.

tected a promising anomoly on a plot of land known as the Kidd 55 segment near Timmins, Ontario, Canada. In November, 1963, TGS core-drilled the anomoly at its "strongest" point. The hole was designated K-55-1 and was completed November 12 at a depth of 655 feet. High ore content was indicated by visual examination, and after the core was split and sent to Utah for assay, it disclosed an average mineral content of 1.18% copper, 8.2% zinc, and 3.94 ounces of silver per ton, over a length of 602 feet. In response to the preliminary results, the TGS chief geologist wrote in a November 14, 1963, memorandum that this was "obviously of ore-grade"[3] but that "a great deal of caution must be exercised in extrapolating this intersection to tonnage estimates."

At this stage of the operations TGS owned only a fraction of the Kidd 55 property. Extreme precautions were taken to the end that no outsider would gain knowledge of the results of the explorations. By March, 1964, TGS had acquired without difficulty substantially all interest in the promising acreage adjacent to the drill site.

On April 7, 1964, K-55-3 was completed. The mineral content, by visual examination of the core, compared favorably with K-55-1 and eliminated the chances that the latter had been drilled "down dip". This hole aided in roughly establishing the east-west boundaries of the sulfite ore body. K-55-4 was completed to a 578 foot depth by 7:00 p.m., April 10, and produced a core comparable to K-55-1 and -3. K-55-4 had been drilled 200 feet south of K-55-1, on a 45 degree angle toward the west. Holes K-55-5 and K-55-6 had been started and were drilling by 7:00 p.m., April 10. K-55-5, 200 feet north of K-55-1 and on a 45 degree angle to the west, had encountered substantial copper mineralization over 42 feet of the 97 feet then drilled. K-

3. "Ore" is a word of art which indicates a body of commercially minable minerals.

55-6, 300 feet east of K-55-1 and on a 60 degree angle to the west, had encountered substantial copper mineralization over the last 127 feet of the 569 foot hole.

Between 7:00 p.m., April 10 and 7:00 p.m., April 12 (the evening prior to the first release) more data became available. K-55-5 was at the 531 foot level and had continued to encounter substantial copper mineralization over that entire length. During the same interval, K-55-6 had reached a depth of 881 feet and had found mineralization over the length of this intermediate drilling. Meanwhile, K-55-7 was started approximately 400 feet north of K-55-1 on a westerly 45 degree angle and was at 91 feet and showing mineralization. And K-55-8 was drilling at a depth of 162 feet without report as to its mineral content.

By the morning of April 13, K-55-5 had encountered substantial copper mineralization to the 580 foot mark; K-55-6 had found mineralization to the 946 foot level; and 50 feet of the 137 feet drilled at K-55-7 showed mineralization. By April 16, K-55-1, -2, -3, -4, -5, -6, and -8 were completed, K-55-7 was at 613 feet, -9 was at 373 feet, and -10 was at 123 feet. In a thumbnail sketch, this illustrates the rapid fire manner in which data was being accumulated at the Timmins drill site.

Although TGS sought to suppress the nature and extent of its discovery at Timmins by early 1964, rumors had begun to generate excitement about the alleged strike. By April, 1964, property within several miles of the TGS site had been "staked". Canadian newspapers carried the rumors, and of their effect on the Toronto Stock Exchange, proclaimed by one to be "the wildest speculative spree since Nineteen Fifties." Eventually the rumors worked south to the United States.

On Saturday, April 11, 1964, both the New York Times and the Herald Tribune carried stories on the rumored

strike.[4] In response to the Times and Herald Tribune articles, the president of TGS directed Fogarty to prepare an official TGS statement. The president, a vice president and Fogarty all agreed that they could not responsibly conclude that a commercial ore body existed and that no calculations as to the size of grade of ore could be made without further drilling. Fogarty then drafted a statement based upon data gathered as of 7:00 p.m., April 10, and he released the statement Sunday afternoon, April 12.[5]

4. The Herald Tribune article follows in part:

"The biggest ore strike since gold was discovered more than 60 years ago in Canada has stampeded speculators to the snow-bound old mining city of Timmins, Ontario, some 450 miles northwest of Toronto.

"This time it's copper. Texas Gulf Sulphur Co., Ltd., which reportedly has made an unparalleled find in the Big Water Lake area about 15 miles north of Timmins, would not confirm reports of the strike.

"* * *

"The story of the strike goes something like this: * * * The richness of the copper it [TGS] discovered was so great that samples reportedly were flown out of the country to be assayed.

"The huge lode is supposed to consist of a bed of copper sulfite 600 feet wide with a possible overall copper return of 2.87 per cent through most of its width. * * *

"But the richest yield comes from the first 100 feet of that 600 foot belt. It is supposed to be 5.6 per cent, a bonanza if the story proves more than just a myth. But myth it may be.

"* * *

"PCE Explorations reportedly is the company which worked with Texas Gulf Sulphur to make the strike.

"* * *

"Sources in Timmins said four diamond drilling machines are working on Texas Gulf land, with four more machines slated to begin drilling next week. * * *"

5. "During the past few days, the exploration activities of Texas Gulf Sulphur in the area of Timmins, Ontario, have been widely reported in the press, coupled with rumors of a substantial copper dis-

[*footnote continued on next page*]

*Appendix —Opinion of the Court of Appeals*

By TGS invitation, on April 13, a reporter from a Canadian mining journal, the Northern Miner, visited the Kidd-55 drilling site. The article detailing that visit was published April 16, and indicated that this "must be recorded as one of the most impressive drill holes completed in modern times." That same day, at 10:00 a.m. Eastern Standard Time, Fogarty held a second press conference and released a statement which revealed in some detail the

---

[*footnote continued from preceding page*]

covery there. These reports exaggerate the scale of operations, and mention plans and statistics of size and grade of ore that are without factual basis and have evidently originated by speculation of people not connected with TGS.

"The facts are as follows. TGS has been exploring in the Timmins area for six years as part of its overall search in Canada and elsewhere for various minerals—lead, copper, zinc, etc. During the course of this work, in Timmins as well as in Eastern Canada, TGS has conducted exploration entirely on its own, without the participation by others.

"Numerous prospects have been investigated by geophysical means and a large number of selected ones have been core-drilled. These cores are sent to the United States for assay and detailed examination as a matter of routine and on advice of expert Canadian legal counsel. No inferences as to grade can be drawn from this procedure.

"Most of the areas drilled in Eastern Canada have revealed either barren pyrite or graphite without value; a few have resulted in discoveries of small or marginal sulphide ore bodies.

"Recent drilling on one property near Timmins has led to preliminary indications that more drilling would be required for proper evaluation of this prospect. The drilling done to date has not been conclusive, but the statements made by many outside quarters are unreliable and include information and figures that are not available to TGS.

"The work done to date has not been sufficient to reach definite conclusions and any statement as to size and grade of ore would be premature and possibly misleading. When we have progressed to the point where reasonable and logical conclusions can be made, TGS will issue a definite statement to its stockholders and to the public in order to clarify the Timmins project. * * *".

magnitude of the discovery at Timmins.[6] Summaries of this announcement appeared on the private wire service of Merrill Lynch and on the Dow-Jones wire service shortly thereafter.

6. "Texas Gulf Sulphur Company has made a major discovery of zinc, copper and silver in the Timmins area of Ontario, Canada.

"We announced last Sunday that when Texas Gulf had done sufficient work to reach firm conclusions, the company would issue a definite public statement on the Timmins project. We are now prepared to make that statement.

"Just ten days ago TGS had but one drilling rig operating in this area. As we state in our release of April 12, initial drilling on this one prospect had led to preliminary indications that more drilling would be required for proper evaluation. We immediately moved in additional drills so that by April 12 four drills were operating. With four drills, considerably more data has been accumulated.

"Seven drill holes are now essentially complete and indicate an ore body of at least 800 feet in length, 300 feet in width and having a verticle depth of more than 800 feet.

"We have not yet delimited the ore body in either direction along the strike. We have only drilled to a vertical depth of 800 feet. Values remain consistent to that depth.

"This is a major discovery. Preliminary data indicate a reserve of more than 25 million tons of ore. The only hole assayed so far represents over 600 feet of ore, indicating a true ore thickness of nearly 400 feet. The hole is described as follows:

> "Overburden is 24 feet. The initial core recovered showed 1 per cent copper over 24 feet. This was followed by a heavy chalcopyrite section of 82 feet, which assayed 7 per cent copper, 9.7 per [sic] zinc, and 2.4 ounces of silver. An additional 20 feet of massive sulphide assayed 12 per cent zinc. Disseminated sphalerite occurred through the following 44 feet of rock and this section assayed nearly 5 per cent zinc. A silver-rich zone of 36 feet followed, assaying 0.8 per cent copper, 13 per cent zinc, and 10.5 ounces of silver. An additional 16 feet assayed 4 per cent zinc and over 5 ounces of silver.
>
> "The following 100 feet was zinc-rich and assayed 0.33 per cent copper, 14.3 per cent zinc and 4 ounces of silver. A 106 foot section of core assaying 8 per cent zinc and 7.2 ounces of silver followed 36 feet of massive pyrite, assaying 3.4 per cent zinc, and 4 ounces of silver. A graphitic zone for the following 86

[*footnote continued on next page*]

Reynolds, Mitchell and the Stouts testified that they sold their TGS stock after hearing of the April 12 release but before becoming aware of the April 16 release. Sometime after the first release was published, Reynolds' broker in Salt Lake informed him as to its general content. On April 16, the broker relayed rumors that TGS had made a strike but in the broker's judgment this was mere propaganda. Reynolds then testified that he decided "to get out while the getting was good," whereupon he sold his 500 shares. Later that afternoon he learned of the favor-

---

[*footnote continued from preceding page*]

feet contained approximately 4 per cent zinc and 2 ounces of silver. The final 20 feet assayed 8.3 per cent zinc and 2 ounces of silver. The overall interval of mineralization which could be mined in an open pit operation averaged 1.18 per cent copper, 8.1 per cent zinc, and 3.8 ounces of silver over a core length of 602 feet. The true width of the overall mineral zone is approximately 400 feet.

"Visual examination of cores from the other holes indicates comparable grade and continuity of ore.

"The ore body is at shallow depth, having only some 20 feet of overburden. This means that it can easily be mined initially by the open pit method.

"This discovery is in the northeast part of Kidd Township, and is about ten miles north of the Timmins airport.

"Our land position is favorable. Texas Gulf holds the mineral rights in 70 per cent of Kidd Township and has substantial acreage in the adjacent townships.

"TGS has been exploring in the Timmins area for some six years, using its own geophysical methods, followed by core drilling. Many prospects were drilled before this strike.

"TGS is actively continuing in the area, and in addition to this discovery is presently drilling on another prospect in the same township. We are continuing our exploration and are proud of our small but exceptionally competent exploration staff.

"We are continuing to drill this structure as systematically and rapidly as possible to determine its limits. We hope to have more information concerning this important discovery at the time of our stockholders' meetnig on April 23 in Houston, Texas."

able TGS report. He testified that had he known of the K-55-1 core results he would have doubled his holdings.

Mitchell visited his broker on the afternoon of the sixteenth, at which time he was referred to the April 12 release. He concluded that the stock would not sustain its current rise and gave instructions to sell 400 shares short against the box. Then, realizing he had failed to dispose of 20 shares, he delivered them on the seventeenth with similar sell instructions. According to his testimony, he had no knowledge of the April 16 release when he sold. After hearing about the April 12 release and that the TGS Timmins discovery was overrated, the Stouts gave orders to sell their 1,000 shares on April 21.

This controversy was tried to the court without a jury. On the basis of the testimony and exhibits produced at that trial, the district court made findings of fact and conclusions of law. To the extent that appellants' arguments rest upon a relitigation or reassessment of factual matters, we will defer to the trial court unless we are satisfied that they were clearly erroneous. Rule 52 F.R.Civ.P., 28 U.S.C. Fireman's Fund Ins. Co. v. S.E.K. Construction Co., Inc., —— F.2d —— (10th Cir. 1970); Butler Paper Co. v. Manske-Kenzie Printing Co., 424 F.2d 247 (10th Cir. 1970); Knauff v. Utah Construction and Min. Co., 408 F.2d 958 (10th Cir. 1969).

The trial court found that the press release of April 12 was false, misleading, deceptive and fraudulent with respect to material matters disclosed by the company's drilling efforts; that the authors knew of the presence of ore-grade copper and zinc in major proportions; that the magnitude of the discovery was either misstated or concealed; and that TGS and Fogarty knew the press release statements were incorrect and misleading, and knew or should have known that the statements would be relied upon by shareholders. After finding that each appellee had relied on the April 12 release in selling his TGS stock, the court

awarded damages based on the average of the highest daily per share selling price between April 16, 1964, and May 13, 1964, twenty trading days following the last press release.

Rule 10b-5 is plain, concise and unambiguous. It provides as follows:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (1) To employ any device, scheme, or artifice to defraud,
>
> (2) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (3) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

Neither Rule 10b-5 nor Section 10(b) in terms grants a private right of action for the nonfeasance or malfeasances denoted in their language. But this is of miniscule significance in this litigation, presumably because such right has now been recognized in all the federal circuits which have had occasion to consider the issue.[7]

7. Bank of America National Trust and Savings Association v. Douglas, 105 F.2d 100 (D.C.Cir. 1939); Rogen v. Ilikon Corp., 361 F.2d 260 (1st Cir. 1966); Securities and Exchange Commission v. Texas Gulf Sulphur Co., 401 F.2d 833 (2nd Cir. 1968); McClure v. Borne Chemical Co., 292 F.2d 824 (3rd Cir. 1961); Rekant v.

[*footnote continued on next page*]

From its origin, the private right of recovery has been based on the general principle of tort law that violation of a provision of a criminal statute designed to prevent a particular type of harm can give rise to a civil remedy. Kardon v. National Gypsum Co., 69 F.Supp. 512 (E.D.Pa. 1946). In civil actions instituted on the basis of 10b-5 violations, the keynote of which is fraud, the full panoply of common law fraud elements—misrepresentation or nondisclosure, materiality, scienter, intent to defraud, reliance and causation—have crept in and played varying roles of significance. However, a number of these elements have diminished in importance in private actions, and we have stated in Stevens v. Vowell, 343 F.2d 374, 379 (10th Cir. 1965), that "[i]t is not necessary to allege or prove common law fraud to make out a case under the statute and rule. It is only necessary to prove one of the prohibited actions such as the material misstatement of fact or the omission to state a material fact." Notwithstanding, appellants urge that appellees have failed to establish the presence of most of the common law fraud ingredients, i.e., misrepresentation or nondisclosure of material facts, scienter, intent to defraud, reliance, and some semblance of privity. A full measure of our attention will be devoted to each of these constituent parts.

The misleading, misrepresented or untruthful character of the release may appear from the nature of the statement considered alone, or, when the facts are fully disclosed,

---

[*footnote continued from preceding page*]

Desser, 425 F.2d 872 (5th Cir. 1970); Texas Continental Life Ins. Co. v. Dunne, 307 F.2d 242 (6th Cir. 1962); Jordan Building Corp. v. Doyle, O'Connor & Co., 401 F.2d 47 (7th Cir. 1968); City National Bank of Fort Smith, Ark. v. Vanderboom, 422 F.2d 221 (8th Cir. 1970); Ellis v. Carter, 291 F.2d 270 (9th Cir. 1961); Gilbert v. Nixon, 429 F.2d 348 (10th Cir. 1970); and impliedly in J.I. Case Co. v. Borak, 377 U.S. 426, 84 S. Ct. 1555, 12 L.Ed.2d 423 (1964) and Surowitz v. Hilton Hotels Corp., 383 U.S. 363 (1966).

from the half truths, omissions or absence of full candor concealed therein. *See* Gilbert v. Nixon, 429 F.2d 348, 356 (10th Cir. 1970); Meisel v. North Jersey Trust Company, 218 F.Supp. 274 (S.D.N.Y. 1963); Cochran v. Channing Corporation, 211 F.Supp. 239 (S.D.N.Y. 1962). Misrepresented or omitted facts become material, hence actionable under 10b-5, when, considering the complaining parties as reasonable investors, the disclosure of the undisclosed facts or candid revelation of misleading facts would affect their trading judgment. *See* Gilbert v. Nixon, supra; S.E.C. v. Texas Gulf Sulphur Company, 401 F.2d 833, 849 (2nd Cir. 1968), *cert. den'd sub nom.* Coates & Kline v. S.E.C., 394 U.S. 976 (1969); Rogen v. Ilikon Corporation, 361 F.2d 260, 266 (1st Cir. 1966); List v. Fashion Park, Inc., 340 F.2d 457, 462 (2nd Cir. 1965), *cert. den'd sub nom.* List v. Lerner, 382 U.S. 811 (1965). The implicit variables to be weighed in a materiality analysis are the magnitude and probability of the occurrence of the event, set against the size and total activity of the subject company.

The trial court found the April 12 release "inaccurate, misleading and deceptive with respect to material matters." Reynolds v. Texas Gulf Sulphur Co., 309 F.Supp. 548, 559 (D.Utah 1970). We agree upon the following recitation of facts found in the record.

To put the chronicle of events in perspective, it must be remembered that from the drilling of K-55-1 in late 1963, no serious drilling activity had transpired until March 31, 1964. On the basis of the core analysis then available to them, the corporate leaders committed themselves to secrecy regarding the "prospect" until the adjacent property could be acquired. Once substantial holdings in contiguous realty was accomplished, drilling activity again came to life with renewed vigor. As of April 10, three drilling rigs were operating, with another to begin drilling on April 12, in an obvious effort to ascertain the dimensions of the min-

eral body. Daily reports on drilling progress continuously altered the measurements of the body, but the mineralization content continued to retain the same characteristics as the core from K-55-1. The data available to TGS at the time of the first press release was ample to have accorded with a more complete, thereby favorable, statement. The representation that "preliminary indications [are] that more drilling would be required for proper evaluation of this prospect" was not a statement candidly disclosing the available knowledge of TGS. Although the full magnitude of the ore body could not be precisely determined, the available information allowed more than a marginal possibility that a commercial "mine" existed.

The contested press release was issued during the afternoon of Sunday, April 12, and purported to be based on "work done to date" and "drilling done to date." This misrepresents and distorts the actual fact that the information upon which TGS formulated the release was current as of 7:00 p.m., April 10. Only in light of the rapid progression of available drilling information does this become forcefully significant. Between 7:00 p.m. on Friday and late afternoon the following Sunday, these developments occurred: (1) K-55-5 had been drilled another 471 feet to a depth of 531 feet; (2) K-55-6 had been drilled another 301 feet to a depth of 881 feet; (3) K-55-7 had been commenced and was at the 91 foot level; and (4) K-55-8 had been commenced and was at the 105 foot level. Thus at the time of the release, TGS drilling had established the rough east-west boundaries of the ore body (through K-55-1 and K-55-3) at nearly 300 feet; the zone of ore proceeded south at least 200 feet (K-55-4), strong mineralization was evident 200 feet north (K-55-5) with fair mineralization showing 400 feet north; and the depth was being ascertained (K-55-6) by an 881 foot hole which was still encountering mineralization at that level.

The recitation that "work to date has not been sufficient to reach definite conclusions and any statement as to size and grade of ore would be premature and possibly misleading" is a one-sided statement. No one could dispute that TGS could not have accurately defined the outer limits of the ore body as of April 12, but that is not the test. When TGS undertook to deny and clarify rumor and fact, they were bound to accurately depict the situation as they then knew it. The full magnitude may yet have been a mystery, but armed with the data available on the 12th, TGS was in a position to unveil the then known dimensions and drilling data of their discovery. Having failed to accurately portray what they knew, and commenting that the information was current when in fact it was sorely outdated, TGS misrepresented the facts of the Kidd 55 discovery.

To buttress the findings above, the trial court reiterated that the Northern Miner journalist who was permitted to visit Kidd 55 on April 13 was able to print a detailed story with the approval of TGS.[8] The agreement was that Ackerly would visit the drill site and on the basis of his observation, prepare an article for publication. But it was to be printed only after Mollison, a vice president in charge of the Timmins project, read, edited, and authorized its

8. Texas Gulf Sulphur has chalked up a brilliant exploration success * * * a major new zinc-copper-silver mine is definitely in the making. * * *

* * * On the basis of seven tests either completed or drilling, it can be stated that a strike length of 600 ft. minimum has been established showing an ore width of roughly 300 ft. which has been traced so far to a maximum vertical depth of about 800 ft. * * * This must be recorded as one of the most impressive drill holes completed in modern times.

From the dimensions already known, the Northern Miner can say that something in excess of 10,000,000 tons of ore is indicated. It is capped with something like 20 feet of overburden, presenting no stripping problems; and the steep dip and wide widths will lend themselves ideally to an open-pit mining situation.

printing. Just as the trial court, we believe this confirms the finding that TGS knew a great deal more than it told on April 12 and that by concealing, omitting or misrepresenting these facts they violated Rule 10b-5.

Even if it is for the moment assumed that some notation had been made that the information was not current, the release still was false, misleading and deceptive. The rumors were of a "substantial copper discovery." In effect, TGS answered without qualification that these rumors were "without factual basis." Then they proceeded to speak of most areas drilled as revealing "either barren pyrite or graphite without value; a few have resulted in discoveries of small or marginal sulphide ore bodies." It was then stated that more drilling would be required for proper evaluation. Not a single note of encouragement is contained in the entire April 12 release regarding the Kidd 55 drilling. The trial court found the release painted a bleak and gloomy picture, and we agree. The substance of the release was a complete denial of the rumors, without any attempt to relate the favorable prospects as shown by the core assay of K-55-1 and the visual examinations of cores from K-55-3, -4, -5 and -6. Each core, in its own way, added to the confirmation of an exceptional ore discovery. We do not now decide whether TGS would have had to make a statement on the 12th, absent the rumors. But with the described data available it was deceitful and fraudulent to speak as TGS did.

By the testimony of appellees' expert, on April 12, TGS knew or could have conservatively computed the reserves of Kidd 55 at 7,390,000 tons of ore valued at $183,740,000. And by the evening of April 12, sufficient data was available for TGS to calculate the reserves at 11,790,000 tons valued around $219,740,000. When the trial court, crediting this testimony over that tendered by appellants' expert, put those figures alongside the computation made in

the Northern Miner based on April 12 data indicating in excess of 10,000,000 tons, its finding as to inaccuracy and deception are well substantiated and thus sustained.

Appellants seek to diminish the credibility of appellees' expert, Dr. Christiansen, by pointing to his method of evaluating the reserves, by urging that his conclusions were based on post-April 10 drilling information and took into account the April 16 release, and it is charged that contemporaneous remarks made by the judge during trial served to discredit Dr. Christiansen's calculations. Addressing the last allegation first, the trial judge ultimately viewed Dr. Christiansen's testimony as credible and notwithstanding the contrary trial colloquy, we are bound by that unless there was clear error. Second, the method employed by appellees' expert did not deviate from professional norms and the proof of that is unerringly highlighted by the content of the April 16 release. Simply because one expert is willing to compute ore reserves upon given data where another refuses, does not destroy the credibility of the first nor improve the reliability of the latter. Dr. Christiansen carefully progressed through the daily series of test cores, logs, etc., and upon the then available data, computed the reserves on the basis of each day's drilling. We can find no error in trusting these computations.

These facts also provide ample foundation for the trial court's finding of materiality. K-55-1 had been assayed and was known to contain minerals of extraordinary quality. The cores from K-55-3 and K-55-4 were visually appraised to be of the same high quality, and the preliminary results of K-55-5, -6 and -7 expanded the limits of the ore body to commercially minable proportions. Additionally, the ore was near the surface to facilitate more economical strip mining. Even considering the size of TGS and its level of operations in international mineral exploration and development, the known size and quality of the ore

body was material information; that is, the trading judgment of reasonable investors would not have been left untouched upon receipt of such information. The trial court was unerringly correct.

TGS seeks refuge in the language of the New York Stock Exchange Company Manual which provides that in the face of rumors without factual basis or rumors which need clarification or interpretation, a quick and speedy denial is the recommended procedure.[9]

It would be an unwarranted contortion of this rule to enfold TGS within its protection. First, because of the facts heretofore set forth, it cannot be said that the rumors had no basis in fact. Second, an S.E.C. statement, relied upon by TGS to support their proposition, is contrary to the facts of this case. Directing its attention to rumors circulating about the Alaskan North Slope oil drilling activities, the Commission has warned investors against those rumors because of the intricacies and uncertainties of oil production on the North Slope. The S.E.C. has cautioned the oil companies "to weigh carefully the conclusions and interpretations of information they may use in statements released to the public." TGS has seized onto this language as a characterization of the action they took. But the S.E.C. continued: "While the absence of proved reserves does not preclude *factual disclosures* of exploratory activities, *such as information relating to drilling operations*, any statements which are made should be appropriately qualified to indicate the limitations upon the significance of the facts disclosed." [Emphasis added.]

9. "Occasions may arise when rumors have been circulated which have no basis in fact or which require clarification or interpretation and also which result in unusual activity or price changes in a particular security. Under such circumstances, the most effective procedure is the quick and speedy denial of such rumors through a release to the public press." [A-22]

The duty evolving upon a company facing these circumstances is to speak truthfully, accurately and with total candor as to the material facts. That is not too much to ask of any company with the interest of its shareholders central to its commentary. It is what the S.E.C. demands, what the law requires, and what every stockholder is entitled to. Sunray DX Oil Company v. Helmerich & Payne, Inc., 398 F.2d 447 (10th Cir. 1968), does not forbid this reasoning. In the context of the facts there present, the court felt that a detailed statement would not add to the informed status of investors, but would mislead them due to the nuances of technical terms used in divulging further information. The problems extant in that off-shore drilling case are not present in the instant controversy.

It is said that if the courts require factual data in statements such as that originally framed by TGS, issuance of statements will fall out of favor and use. The conjecture is that by requiring a complete statement of material facts, corporations will cease to issue them and the Act will be frustrated in its attempt to keep stockholders informed of material facts. We view this speculation untenable, for the duty to disclose facts when they become material has not been altered by this decision. Simply stated, when the material information is available and ripe for publication, the difficulties inherent in formulating a release cannot overbear the accuracy of the statements contained therein. Nor is it reasonable to conclude that the detail of a full release will preclude its publication in these circumstances. Indeed, the thoroughness of the April 16 release stands as evidence to the contrary.

Another argument of appellants is that as a predicate to a 10b-5 action, the corporation, its directors or other "insiders" must be trading in the market.[10] At minimum,

10. Although considerable trading had been done in the market by corporate "insiders" and "tippees", it was stipulated at trial that there was no illegal trading by the instant parties at or after the time of the April 12 release.

it is urged that a market purpose to benefit the alleged wrongdoer must be proven before recovery can be permitted. The attempt is to circumvent the language in SEC v. Texas Gulf Sulphur Company, 402 F.2d at 862: "Rule 10b-5 is violated whenever assertions are made * * * in a manner reasonably calculated to influence the investing public, e.g., by means of the financial media * * * if such assertions are false or misleading or are so incomplete as to mislead irrespective of whether the issuance of the release was motivated by corporate officials for ulterior purposes. It seems clear, however, that if corporate management demonstrates that it was diligent in ascertaining that the information it published was the whole truth and that such diligently obtained information was disseminated in good faith, Rule 10b-5 would not have been violated."

In its origin, 10b-5 was intended only to give sellers the same protection extended to buyers by other provisions of the Act, and did not contemplate protection of stockholders against a breach of fiduciary duty by corporate insiders. Within a few years, however, the federal courts ceased to look upon the Rule in the narrow context of seller protection and began to see in it a greater purpose, i.e., equalization of bargaining position of the parties on both sides of a transaction. A. Bromberg, Securities Law: Fraud—S.E.C. Rule 10b-5, §3.2 (200), (300), pp. 65-66 (1969) [hereinafter Bromberg]. But even with this expanded vision, the courts generally required, at minimum, "[a] semblance of privity between the vendor and purchaser of the security in connection with which the improper act, practice or course of business was invoked. * * *" Joseph v. Farnsworth Radio & Television Corp., 99 F.Supp. 701, 706 (S.D.N.Y. 1951).

The Second Circuit in the Texas Gulf Sulphur case expanded this rationale to include protection for open market investors, including speculators, when misled by nontrad-

ing insiders. After reviewing Congressional history, the court said: "Congress when it used the phrase 'in connection with the purchase or sale of any security' intended only that the device employed, whatever it might be, be of a sort that would cause reasonable investors to rely thereon, and, in connection therewith, so relying, cause them to purchase or sell a corporation's securities. * * * We do not believe that Congress intended that the proscriptions of the Act would not be violated unless the makers of a misleading statement also participated in pertinent securities transactions in connection therewith, or unless it could be shown that the issuance of the statement was motivated by a plan to benefit the corporation or themselves at the expense of a duped investing public." S.E.C. v. Texas Gulf Sulphur Company, 401 F.2d at 860. TGS invites this circuit to either part company with the Second Circuit rationale or distinguish it on the basis that it must be confined to S.E.C. enforcement actions.

The Second Circuit has laid to rest the argument that the new "connection" requirement be narrowly applied to S.E.C. enforcement actions. Following the TGS suit was Hiet v. Wietzen, 402 F.2d 909 (2nd Cir. 1968), a private action, wherein the TGS "connection" rule was applied. We also decline the invitation to ignore the forward looking view of the Second Circuit regarding the "connection" requirement. Perhaps the first step is to realize that the common law requirement of privity has all but vanished from 10b-5 proceedings[11] while the distinguishable "con-

11. Hiet v. Wietzen, 402 F.2d 909 (2nd Cir. 1968); Texas Continental Life Ins. Co. v. Dunne, 307 F.2d 242 (6th Cir. 1962); Rippey v. Denver U. S. National Bank, 260 F.Supp. 704 (D.Col. 1966); Miller v. Bargain City, U.S.A., Inc., 229 F.Supp. 33 (E.D.Pa. 1964); Freed v. Szabo Food Service, Inc. (N.D.Ill., filed Jan. 14, 1964); Bromberg, 38.5 (511) at 207; III Loss, Securities Regulations, Chap. 11C(c) at 1767-71 and VI Loss, Chap. 11C at 3890-97.

nection element is retained.[12] In its development, the cases have deemed the "connection" requirement fulfilled if the company has uttered false or misleading statements concerning the securities in question, provided the complainants have relied on the misrepresented facts. The result which we here support is that insider trading is not a requisite for 10b-5 violation by misrepresentation. As appropriately stated by the Second Circuit, "a corporation's misleading material statement may injure an investor irrespective of whether the corporation itself, or those individuals managing it, are contemporaneously buying or selling the stock of the corporation." S.E.C. v. Texas Gulf Sulphur Company, 401 F.2d at 861. The trial court had little difficulty finding from the testimony of Fogarty and other corporate officers that the April 12 statement was made in a manner reasonably calculated to influence the investing public. We concur.

But even if the release was made in connection with the sale of these securities, appellants further urge that the overwhelming weight of authority holds that scienter in some form is required in a private 10b-5 damage action. *See* VI Loss, Ch. 11C at 3883-90. In the Second Circuit, at least, that description appears to be correct. But while some degree of scienter is required, it does not equate with the intent to defraud required in a common law fraud action. Globus v. Law Research Service, Inc., 418 F.2d 1276 (2nd Cir. 1969); Hiet v. Wietzen, supra; Astor v. Texas Gulf Sulphur Company, 306 F.Supp. 1333 (S.D.N.Y. 1969). Contrariwise, in the Eighth Circuit, City National Bank of Fort Smith, Ark. v. Vanderboom, 422 F.2d 221 (8th Cir. 1970), and the Ninth Circuit, Ellis v. Carter, 291 F.2d 270 (9th Cir. 1961), the rule is that scienter is not required to maintain a private 10b-5 damage action. We have dealt

12. *See* Rippey v. Denver U.S. National Bank, supra; Stockwell v. Reynolds & Co., 252 F.Supp. 215 (S.D.N.Y. 1965); Miller v. Bargain City, U.S.A., Inc., supra.

with the issue under significantly different circumstances in Stevens v. Vowell, 343 F.2d 374 (10th Cir. 1965). But in Gilbert v. Nixon, 429 F.2d 348, 357 (10th Cir. 1970), we considered the identical issue in a case involving Section 12(2) and Rule 10b-5. The rule there articulated is applicable here. "One is not to be held liable * * * because of his misleading misrepresentation or omission of material fact, the truth of the matter being unknown to the purchaser, if the party responsible for the misrepresentation or omission sustains the burden of proving that he did not know, and in the exercise of reasonable care could not have known that it was a misrepresentation or omission."

Two times during his opinion the trial judge recited: "[T]he record here discloses that the press release issued by defendants was misleading, intentionally deceptive, inaccurate and knowingly deficient in material facts." Reynolds v. Texas Gulf Sulphur Company, 309 F.Supp. at 562, 563-64. Confronted with the abundance of evidence in the record, we cannot conclude that TGS sustained its burden of proving that it did not know of the misrepresentation, nor was it demonstrated that with due diligence TGS could not have known of the faultiness of the statement.

The complainants have met the reliance requirement if "the misrepresentation is a substantial factor in determining the course of conduct which results in [the investors'] loss." List v. Fashion Park, Inc., 340 F.2d 457, 462 (2nd Cir. 1965); VI Loss, Ch. 11C at 3876-83. Appellants' argument on this point is two-fold: First, that the trial court's findings that each plaintiff-appellee relied on the April 12 release was clearly erroneous; and, second, that as a matter of law, once the April 16 release was received by the brokerage houses over the Merrill Lynch and Dow-Jones wire services, curative information was available which should have corrected any erroneous notions in the minds of reasonable investors as to the Timmins project.

The trial court specifically found that each of the appellees herein relied upon the misleading and inaccurate announcement in making his decision to sell his TGS stock, and that none knew of the announcement of April 16 at the time of his sale. Reynolds v. Texas Gulf Sulphur Company, 309 F. Supp. at 559, 560, 561, 562. Appellants enumerate several factors which may have induced Reynolds to sell his TGS stock. A thorough search of the record convinces us that although any one or all of the factors may have partially motivated the sale, the evidence is not so deficient as to make the finding of the trial court clearly erroneous that the principal reliance was on the April 12 statement.

The dispute over the Mitchell sale is that he timed his decision to sell on speculation as to what the market was going to do. Again, the evidence of record does not clearly refute the finding that the primary motivation was the deceptive April 12 release. The Stouts' case is more difficult due to the time lapse between the corrective April 16 release and the sell order—more than five days later. But even with that entanglement, we cannot, on the basis of clear error, conclude from the record that the April 12 release was not a substantial factor in the Stouts' decision to sell.

Greater difficulty is encountered with the second of appellants' two-pronged argument which directs itself to the issue of due diligence and good faith required of investors trading in the market. *See* City National Bank of Fort Smith, Ark. v. Vanderboom, supra. Reynolds traded within a reasonably brief time following the April 16 release and should not be denied his recovery. Mitchell is in exactly the same position with regard to the 400 shares which were sold by April 17. Both testified that they were attempting to reap the maximum profit before the "gloomy" release took its toll. We conclude that good faith and due dili-

gence were exercised in the sale of these shares. On the other hand, although mala fides is not involved, the record will not support a claim of due diligence in the Stouts' sale and in Mitchell's late sale of the 20 shares.

At some point in time after the publication of a curative statement such as that of April 16, stockholders should no longer be able to claim reliance on the deceptive release, sell, and then sue for damages when the stock value continues to rise. This is but a requirement that stockholders too act in good faith and with due diligence in purchasing and selling stock. Although Mitchell alleges that he ordered the 20 shares sold on the 17th, there is no dispute that they were not in fact sold until the 23rd. His explanation is that somehow the sell order was not properly communicated until the 22nd, when he called his broker to inquire into their status. In the Stouts' case, there was no miscommunication. They simply did not intend to sell until the 21st. While in some circumstances such delays may not be unreasonable, we conclude that under the circumstances of this case it would unjustifiably extend TGS liability to intolerable limits.

Between April 13 and April 22, TGS stock had increased in value from 30⅛ to a high of 47, with the volume of sales going from 126,500 to over 326,000. But most significant is the abundance of publicity given the April 16 statement during the following few days. The business news of every major news publication carried the story with bold headlines. Indeed, the 45 pages of press clippings and stock quotations in the record gives force to the proportion that the April 16 release received saturation coverage. We conclude that by Wednesday, April 22 when the Stouts sold their stock, and Thursday, April 23 when Mitchell sold the 20 shares, the reasonable investor would have become informed of the April 16 release and could no longer rely on the earlier release in selling TGS stock.

The final defense asserted by appellants is directed to the applicable statute of limitations. There is no statute of limitations contained in Section 10(b) of the Act. The settled rule is that when a federal statute is silent as to the statute of limitations, the appropriate period of limitation of the forum state is applied. United Automobile Workers v. Hoosier Cardinal Corporation, 383 U.S. 696 (1966). The trial court in this case looked to Utah law and applied 78-12-26(3), Utah Code Annotated, 1953: "Within three years: * * * (3) An action for relief on the ground of fraud or mistake; but the cause of action in such case shall not be deemed to have accrued until the discovery by the aggrieved party of the fact constituting fraud or mistake."

Appellants contest the applicability of this fraud statute of limitations upon the tenet that this is not a fraud case. It is apparent, we trust, from the earlier statements in this opinion supporting the findings of the trial court, that the central issues in private 10b-5 damage actions coalesce with "fraud or mistake". Moreover, in Chiodo v. General Waterworks Corporation, 380 F.2d 860 (10th Cir. 1967), it was held that the Utah statute of limitations pertaining to fraud controlled the filing of a complaint under Section 10(b) of the Act. Vanderboom v. Sexton, 422 F.2d 1233 (8th Cir. 1970), is principally distinguishable because that circuit has abrogated any semblance of scienter in a private 10-b-5 damage action. Not having accomplished that same rationale in this circuit, we will here adhere to earlier decisions applying fraud statutes of limitations.

Some doubt still remains, however, whether appellees met this period of limitations. Reynolds filed suit July 12, 1966. No complaint is raised as to the appropriateness of his action meeting the three-year limit. But Mitchell did not file until April 17, 1967, and appellants claim that since he knew of the April 16 release on the date of its issuance, he knew of the fraud on that same day and is thus

not within the time limit for filing suit. Mitchell contended he did not know of the fraud until later. The matter rests on facts which the trial court found favorable to Mitchell, and we sustain that finding on an absence of clear error.

We pass now to the issue of damages. The trial court, in framing a rule for determining a proper award of damages, started with the proposition that the aim of courts in this situation is to restore claiming parties to the positions they would have enjoyed had they not been fraudulently induced to sell their stock. Proceeding to fashion a remedy which would make effective the Congressional purpose, J. I. Case Co. v. Borak, 377 U.S. 426, 433 (1964), the trial court adopted a qualification of the rule announced in Galigher v. Jones, 129 U.S. 193, 201 (1889): "[T]he true and just measure of damages in these cases is to be the intermediate value of the stock between the time of its conversion and a reasonable time after the owner has received notice of it to enable him to replace the stock." From this rule the trial court postulated the following measure of damages: "* * * this is an attempt to give a twenty trading day period within which the average of the highest daily prices is the measure of damages, and a period within which the shareholders received, or should have received, notice of the Texas Gulf Sulphur announcement of April 16." Reynolds v. Texas Gulf Sulphur Company, 309 F.Supp. at 563. With the lapse of twenty trading days it was felt that market reactions would more accurately reflect actual value and allow a reasonable time for the reasonable and diligent shareholder to learn of the April 16 announcement and protect his interest. The averaging aspect was inserted because the trial court felt it highly improbable that any of the appellees would have sold at the highest price.

All party litigants are dissatisfied with this measure of damages. Appellants contend that only actual damages based on market value as of April 16 are recoverable; that

appellees have failed to prove such loss; and even accepting the lower court's measure, twenty days is too lengthy and thereby unreasonable. By cross-appeal, Mitchell and Reynolds request restitution or damages equivalent to restitution, and costs of conducting this action.

We are in harmony with the rudiments of the trial court's measure of damages and alter that rule only to more closely adhere to the notion that the injured parties should be restored to their former status. The divergent approaches taken by the litigants verify the suspicion that a set rule of damages has not been tested in this kind of case. Furthermore, because of the uniqueness of the litigation, it would be unwise to set forth a uniform rule with broad applications to all securities cases. Thus, the rule styled by this court is fashioned for these unprecedented circumstances.

Restitution and damages equivalent to restitution are inappropriate remedies in this action. Traditionally these theories have been concerned with direct-personal dealings in which there is privity and/or unjust enrichment upon which to justify the remedy. Speed v. Transamerica Corporation, 135 F.Supp. 176 (D. Del. 1955), *aff'd modifying interest* 235 F.2d 369 (3rd Cir. 1956); Janigan v. Taylor, 344 F.2d 781 (1st Cir. 1965); Bromberg, §9.1 at 225, et seq. Here neither element is present inasmuch as neither TGS nor Fogarty purchased appellees' shares of stock. The absence of those fundamental facts, plus the hardship it would visit upon TGS as a corporation,[13] makes this case inap-

13. In their appellate brief, appellants claim that if the measure of damages theory applied in the trial court is upheld on appeal, damages will approach $14,000,000. In Ruder, Texas Gulf Sulphur —The Second Round, 63 Nw. U. L. Rev. 423, 428-29 (1969), restitution damages are computed: "* * * if liability is imposed upon TGS in the private suits for the company's failure to disclose the material inside information which it possessed, its damages may be equal to $130 for every share traded during the period from No-

[*footnote continued on next page*]

propriate for any form of restitution, and the trial court properly rejected it.

We believe the measure of damages used should award the reasonable investor the amount it would have taken him to invest in the TGS market within a reasonable period of time after he became informed of the April 16 release. Through the testimony of both Reynolds and Mitchell we are satisfied, as was the trial court, that they possessed ample sophistication to fall within the nebulous reasonable investor category. By Monday, April 20, the diligent and reasonable investor was informed of the most recent TGS statement and as we earlier stated, after that duration a reasonable investor would not have relied upon the April 12 statement in selling his TGS stock. After the reasonable stockholder had opportunity to apprise himself of the April 16 release and its import to investment, a reasonable time lapse may be allowed to expire to permit the investor to decide whether or not he would reinvest and take advantage of a spiraling market. If he has failed to reinvest, as both Reynolds and Mitchell did, he must suffer the consequences of his own judgment. The award proposed would permit one to "cover" by reinvestment and suffer neither loss nor forced sale.

The damages then should be based on the highest value of TGS stock between Monday, April 20 and a reasonable time thereafter. Whether we conclude such duration should be an added nine trading days (through Friday, May 1)

---

[*footnote continued from preceding page*]

vember 12, 1963, through April 16, 1964. Since approximately 3 million TGS shares were traded during this period, damages would amount to over 390 million dollars, approximately 150 million dollars more than the present net worth of the company. If liability is imposed upon TGS only for the period from April 12, 1964, * * * until April 16, 1964, * * * the company could incur damages of about 84 million dollars, since approximately 691,000 shares were traded during that four day period." [Footnotes omitted]

which seems more reasonable in these circumstances, or the seventeen additional trading days imposed by the trial court (through Wednesday, May 13) is irrelevant to the award. For in either event, the highest value was achieved on Wednesday, April 29 (at $59) prior to the expiration of either time limit.

The averaging aspect is deleted to conform with what is considered the focal purpose: to award the reasonable investor an amount which offsets any loss he suffered by a deceitfully induced sale. To award an average price would not fully compensate him for a number of the days within the reasonable period following the last release. While this is an admitted compromise between the restitution rule and the actual damage approach as taken by TGS, it seems a fair way to reinstate stockholders who were wrongfully deprived of their gain because of the deceitful release and, at the same time, deny recovery to those who suffered only by their own lack of due diligence. In selecting the highest daily price the advantage works, to a greater degree, against TGS. But where, as here, the injury is suffered by an act making difficult the exact computation of damages, the wrongdoer is not heard to complain. For "it would be a perversion of fundamental principles of justice to deny all relief to the injured person, and thereby relieve the wrongdoer from making any amend for his acts." Story Parchment Co. v. Patterson Paper Co., 282 U.S. 555, 563 (1931).

In their cross-appeal, Reynolds and Mitchell also argue in favor of awarding attorneys' fees. We are cited to our decisions in Esplin v. Hirshi, 402 F.2d 94 (10th Cir. 1968), *cert. den'd* 394 U.S. 928 (1969), and Estate Counseling Service, Inc. v. Merrill Lynch, Pierce, Fenner and Smith, 303 F.2d 527 (10th Cir. 1962). It is contended that both decisions stand for the proposition that the policy in the federal courts is to award the costs of conducting the action

in securities cases. Although in both cases we allowed recovery of "other outlay legitimately attributable to the defendant's fraudulent conduct," it was not intended to include the costs of bringing the action. This is seen in the Estate Counseling Service case where a defrauded buyer brought the appeal but was not awarded attorney fees as "other outlay legitimately attributable to the defendant's fraudulent conduct." Attorneys' fees are denied.

The damages awarded to Reynolds amount to $12,687.50; Mitchell's damages are fixed at $7,600.00. The decisions by the trial court that both appellees are to receive interest computed at six per cent per annum from the time of sale until the date of the trial court's judgment, and that when recovery is gained from TGS, appellees' claims against Fogarty will be deemed paid, satisfied and discharged, are not disturbed.

Fogarty asserts on his own behalf that the trial court lacked personal jurisdiction over him. Section 27 of the Securities Exchange Act of 1934, 15 U.S.C. §78aa, provides that "[t]he district courts of the United States * * * shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce liability or duty created by this chapter or the rules and regulations thereunder. * * *" The remainder of that statute provides for service of process, allows for review of judgments and decrees, and designates proper venue. The latter provision relates back to the jurisdictional portion, and allows such actions to be brought in any district where the defendant is found or is an inhabitant or transacts business.

The brunt of Fogarty's allegations is directed at venue —not jurisdiction. His main claim is that he has never been an inhabitant of Utah, was not found in Utah, and transacts no business in that state. That was the identical issue posed to this court in Texas Gulf Sulphur Company v. Ritter, 371 F.2d 145, 148-49 (10th Cir. 1967), wherein

we said: "venue as to both defendants will lie in the Utah District if any of the acts or transactions complained of took place in that district." The acts and transactions complained of which have now been proved were "publication of news releases and acts incident to the sale of the stock referred to herein * * * the release of a false and fraudulent press release, upon which he [Reynolds] relied after reading the same in the Wall Street Journal in Salt Lake City, which newspaper had been transmitted to him through the United States mails. In addition the plaintiff contends this press release came to Salt Lake City on the Dow-Jones broad tape." Thus the issue has been decided against Fogarty and is not now open to relitigation.

The only issue left to be decided is raised individually by Reynolds and concerns whether Rule 23 F.R.Civ. P., 28 U.S.C., should be applied to afford relief to all persons who sold TGS stock between April 12 and April 16, 1964. A number of independent inquiries are included in this argument, e.g., may an appellate court correct a class ruling after a decision on the merits; and may parallel class actions be conducted in two jurisdictions? But ignoring all collateral issues, as cross-appellant has invited us to do, the only issue is whether the trial court properly exercised its discretionary powers.

Rule 23(a) recites four prerequisites to a class action. Assuming, arguendo, that the elements of (a) have been met, it appears that the trial court was convinced that a class action in Utah would not conform to (b)(3) of Rule 23. That subsection requires, inter alia, that the class action be "superior to other available methods for the fair and efficient adjudication of the controversy." The Rule outlines four nonexhaustive matters which are to be considered in deciding the superiority of a class action: "(A) the interest of members of the class in individually controlling the prosecution or defense of separate actions;

(B) the extent and nature of any litigation concerning the controversy already commenced by or against members of the class; (C) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; and (D) the difficulties likely to be encountered in the management of a class action." In an opinion reported at 309 F.Supp. 566 (D.Utah 1970), the trial court denied the motion for a class action, basing the decision on Rule 23 (b) (3)(B), (C) and (D).

The trial judge recited that as of October 22, 1969, ninety-four actions had been brought against TGS and individual defendants; that in March, 1969, two actions in the Southern District of New York had been allowed to proceed as class actions; that pursuant to that ruling, tedious and time consuming discovery had taken place; and that if the various private suits were concentrated for trial in a single district, it should be in the Southern District of New York. In summary, he stated: "The litigation in New York is far advanced, far and away the bulk of the cases are there, and the information necessarily to be obtained from the brokerage offices is more readily and more conveniently available in New York City." Reynolds v. Texas Gulf Sulphur Company, 309 F.Supp. at 570. Our conclusion is that the trial court has wisely exercised its discretion.

In No. 280-70, the judgment is affirmed in all respects except as to the untimely sale of the 20 shares and as to the issue of damages. In No. 282-70, the judgment is affirmed in all respects except as to the issue of damages. Accordingly, No. 280-70 is remanded with directions to enter judgment for Mitchell for $7,600.00; and No. 282-70 is remanded with directions to enter judgment for Reynolds for $12,687.50. In No. 284-70, the judgment is reversed and the case is remanded with directions to enter judgment in favor of Texas Gulf Sulphur Company, et al. The cross-appeals in Nos. 281-70, 283-70 and 285-70, are denied.

## Judgment of the United States Court of Appeals for the Tenth Circuit

MARCH TERM—APRIL 26, 1971

Before Honorable David T. Lewis, Chief Judge, and Honorable Delmas C. Hill and Honorable Robert H. McWilliams, Circuit Judges.

[SAME TITLE]

These consolidated cases came on to be heard on the record on appeal from the United States District Court for the District of Utah, and were argued by counsel. On consideration whereof, it is ordered as follows:

In case No. 280-70, the judgment of said district court is affirmed in all respects except as to the untimely sale of the 20 shares and as to the issue of damages.

In Case No. 282-70, the judgment of the said district court is affirmed in all respects except as to the issue of damages.

Accordingly, in case No. 280-70 the cause is remanded with directions to enter judgment for Mitchell for $7,600.00; and in Case No. 282-70, the cause is remanded with directions to enter judgment for Reynolds for $12,687.50.

In Case No. 284-70, the judgment of said district court is reversed and the case is remanded with directions to enter judgment in favor of Texas Gulf Sulphur Company, et al.

The cross-appeals in Nos. 281-70, 283-70 and 285-70, are denied.

/s/ HOWARD K. PHILLIPS

HOWARD K. PHILLIPS, Clerk.

## Order of the United States Court of Appeals for the Tenth Circuit on Petition for Rehearing

JULY TERM—SEPTEMBER 10, 1971

Before Honorable David T. Lewis, Chief Judge, and Honorable Delmas C. Hill and Honorable Robert H. McWilliams, Circuit Judges.

Nos. 281-70 and 283-70

GEORGE GORDON REYNOLDS and WALTER A. MITCHELL,
*Cross-Appellants,*

*v.*

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
*Cross-Appellees.*

Cross-Appellant, Reynolds, has filed a Petition for Rehearing urging two points, neither of which goes to the merits of the case. First, he asks us to assess as costs in the case certain fees paid by him to expert witnesses. As a general rule, such fees in excess of the statutory allowance for fees, mileage and subsistence, are not taxable as costs. In some cases, courts, in the exercise of their general equitable powers, have permitted such allowances in cases involving exceptional circumstances, and in those cases the orders of allowance were made prior to time the witnesses testified. 6 Moore's F.P. 1367. In this case, the trial judge declined after trial to make such an allowance.

We are unable to conclude that the trial judge abused his equitable discretion in denying the allowance and affirm the trial judge in this respect.

By the second point, the petition asks us to supplement our opinion to expressly state that our denial of a class action for Reynolds does not preclude the possibility of other persons in the alleged class from bringing actions in any court having jurisdiction, either in their own behalf or under Rule 23. We see no necessity for such a supplement to our opinion and decline the request.

Accordingly, the petition for rehearing is denied.

LIBRARY
SUPREME COURT, U. S.

Supreme Court, U.S.
FILED
1971
E. ROBERT SEAVER, CLERK

IN THE

# Supreme Court of the United States

October Term, 1971

No. 71-693

GEORGE GORDON REYNOLDS and
WALTER A. MITCHELL,

*Petitioners,*

*against*

TEXAS GULF SULPHUR COMPANY and
CHARLES F. FOGARTY,

*Respondents.*

**On Petition for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit**

## BRIEF OF RESPONDENTS IN OPPOSITION

ORISON S. MARDEN
*Attorney for Respondents*
14 Wall Street
New York, New York 10005

CALVIN A. BEHLE
KEITH E. TAYLOR
PARSONS, BEHLE & LATIMER

P. B. KONRAD KNAKE
THOMAS MCGANNEY
JEFFREY A. BARIST
W. NEIL THOMAS III
WHITE & CASE

*Of Counsel*

# TABLE OF CONTENTS


| | PAGE |
|---|---|
| Questions Presented | 2 |
| Additional Federal Rule Involved | 3 |
| Statement of Facts | 4 |
| Argument | |
| I—This action was inappropriate for class action treatment | 15 |
| A. The Rule 23 motions before trial | 16 |
| B. The motion for class status after the decision in favor of petitioners was required to be denied under the clear language of the Rule | 19 |
| C. The rulings below were required by the provisions and purposes of amended Rule 23 | 21 |
| 1. The authorities under former Rule 23 do not provide a basis for now declaring the *Reynolds* case to be a class action | 22 |
| 2. The prosecution of simultaneous class actions would have been improper | 24 |
| 3. Difficulties inherent in managing a class action inevitably entail time-consuming procedures | 27 |
| D. Petitioners' forays outside their chosen forum | 28 |
| 1. The inapplicability of the Multidistrict Litigation Act | 28 |
| 2. Petitioners' attempts to participate in the New York class action proceedings | 29 |
| II—The courts below correctly refused petitioners' claim for counsel fees | 31 |
| Conclusion | 32 |

## TABLE OF AUTHORITIES


PAGE

***Cases:***

Fleischmann Distilling Corp. v. Maier Brewing Co., 386 U.S. 714 (1967) ..... 31

J. I. Case Co. v. Borak, 377 U.S. 426 (1964) ..... 31

Mills v. Electric Autolite Co., 396 U.S. 375 (1970) ..... 31

Partridge v. Martin, 102 F. 2d 284 (8th Cir.), *cert. denied*, 307 U.S. 644 (1939) ..... 25

Smith v. Swormstedt, 16 How. [57 U.S.] 288 (1853) ..... 23n

Sprague v. Ticonic National Bank, 307 U.S. 161 (1939) 31

Saltzman v. Technicolor, Inc., 51 F.R.D. 178 (S.D.N.Y. 1970) ..... 31

Supreme Tribe of Ben Hur v. Cauble, 255 U.S. 356 (1921) ..... 22, 23, 25

***Statutes and Rules:***

Fed. R. Civ. P. 23 ..... 2, *passim*

Securities Exchange Act of 1934:
Section 10(b), 15 U.S.C. §78j(b) ..... 2, 4, 8
Rule 10b-5 (17 C.F.R. §140.10b-5) ..... 4

28 U.S.C. §1404 ..... 5

28 U.S.C. §1407 ..... 25, 28, 29

***Other Authorities:***

Advisory Committee Notes to Proposed Amendments to Rules of Civil Procedure, 39 F.R.D. 73 (1966) ..... 20, 24, 25, 28

MOORE, FEDERAL PRACTICE (2d ed. 1963) ..... 24

RESTATEMENT, JUDGMENTS (1942) ..... 23n

IN THE

# Supreme Court of the United States

October Term, 1971

No. 71-693

GEORGE GORDON REYNOLDS and WALTER A. MITCHELL,
*Petitioners,*

*against*

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
*Respondents.*

**On Petition for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit**

## BRIEF OF RESPONDENTS IN OPPOSITION

This brief is submitted in opposition to the petition for a writ of certiorari to the United States Court of Appeals for the Tenth Circuit filed by George Gordon Reynolds and Walter A. Mitchell on November 22, 1971. The petition is addressed to the same decision of the Tenth Circuit that is before the Court upon petition for certiorari in Docket No. 71-421. Petitioners herein (respondents in No. 71-421) seek review of two aspects of the judgment below. These issues relate to (1) the exercise of discretion by the United States District Court for the District of Utah in refusing to declare the *Reynolds* action to be a class action for the *Texas Gulf Sulphur Company* litigation,

and (2) the denial of counsel fees and expenses to petitioners' attorneys.

In their petition in No. 71-421, respondents herein have demonstrated the importance of the fundamental issues of liability in this case. We do not deny that there are procedural issues under Fed. R. Civ. P. 23, as amended by this Court in 1966, which have not been decided by this Court. We do submit, however, that the peculiar procedural posture of the *Reynolds* case within the context of the whole *Texas Gulf Sulphur* litigation renders this case an unsuitable vehicle for consideration of the problems arising under Rule 23. Moreover, as demonstrated *infra*, several of petitioners' complaints relate not to the Utah proceeding, but to the conduct of the New York litigation, of which petitioners here have no standing to complain.

## Questions Presented

1. Did the United States District Court for the District of Utah abuse its discretion by denying to this case the status of a class action under Rule 23(b)(3) when the *Texas Gulf* litigation was concentrated in the Southern District of New York, where over 50 similar suits including more than 32 purported class actions were pending, and this case was the only action pending in the federal courts apart from that coordinated litigation?

2. In the absence of any statutory authority, is a plaintiff in an action prosecuted under §10 (b) of the Securities Exchange Act who recovers damages for himself individually entitled additionally to counsel fees and reimbursements of expenses from the defendants?

## Additional Federal Rule Involved

Federal Rule of Civil Procedure 23(c), not set forth by petitioners, provides in relevant portions as follows:

> "(c) DETERMINATION BY ORDER WHETHER CLASS ACTION TO BE MAINTAINED; NOTICE; JUDGMENT; ACTIONS CONDUCTED PARTIALLY AS CLASS ACTIONS.
>
> "(1) As soon as practicable after the commencement of an action brought as a class action, the court shall determine by order whether it is to be so maintained. An order under this subdivision may be conditional, and may be altered or amended before the decision on the merits.
>
> "(2) In any class action maintained under subdivision (b)(3), the court shall direct to the members of the class the best notice practicable under the circumstances, including individual notice to all members who can be identified through reasonable effort. The notice shall advise each member that (A) the court will exclude him from the class if he so requests by a specified date; (B) the judgment, whether favorable or not, will include all members who do not request exclusion; and (C) any member who does not request exclusion may, if he desires, enter an appearance through his counsel.
>
> "(3) The judgment in an action maintained as a class action under subdivision (b)(1) or (b)(2), whether or not favorable to the class, shall include and describe those whom the court finds to be members of the class. The judgment in an action maintained as a class action under subdivision (b)(3), whether or not favorable to the class, shall include and specify or describe those to whom the notice provided in subdivision (c)(2) was directed, and who have not requested exclusion, and whom the court finds to be members of the class."

* * *

## Statement of Facts

Proper consideration of the issues posed by the petition herein requires an understanding of the position of this case within the context of the entire *Texas Gulf Sulphur* litigation. In the history of this complex and precedent-shattering litigation, petitioners Reynolds and Mitchell are late arrivals.

On April 16, 1964, Texas Gulf announced the discovery of a major ore body near Timmins, Ontario, Canada. Approximately one year later, on April 19, 1965, the Securities and Exchange Commission filed a complaint in the United States District Court for the Southern District of New York charging Texas Gulf with violating Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 when it promulgated a press release on April 12, 1964, commenting upon rumors regarding its exploration program. The SEC also charged that certain officers, directors and employees of the Company violated Rule 10b-5 in purchasing TGS stock with knowledge of undisclosed drilling results.*

In the first four months after the filing of the *SEC* suit, more than forty actions seeking private damage recovery were brought against Texas Gulf and various of its officers, directors and employees. A year after the *SEC* complaint had been filed, more than ninety private actions were pending.

---

* We cannot accept petitioners' version of the underlying facts as set forth in their statement of the case (Pet., p. 5), but respectfully refer the Court to the petition in No. 71-421 for a description of those facts and issues.

Most of these actions were commenced in the United States District Court for the Southern District of New York where Texas Gulf has its executive offices and where most of the individual defendants worked. Thirty-two of the cases brought in that court in 1965 purported to be class actions. United States District Judge Dudley B. Bonsal was appointed to coordinate the proceedings in all of the private damage actions (including the alleged class actions).*

In addition to the New York cases, a number of cases were commenced in federal and state courts in other jurisdictions. Where possible, state cases were removed to federal courts, and pursuant to 28 U.S.C. §1404(a), cases pending in the federal courts of Connecticut, Illinois, California, Florida and Texas were transferred to the Southern District of New York. These cases were also assigned to Judge Bonsal for coordination.

By an order dated September 7, 1965, Judge Bonsal provided for an expedited discovery schedule in the *SEC* case, with the product of that discovery to be made available to all of the private plaintiffs. Both the SEC and Texas Gulf produced hundreds of documents, answered numerous interrogatories and requests for admissions, and took pre-trial depositions, all of which were made available to the attorneys in the private actions. In May of 1966, slightly more than a year after the complaint had

* Seventeen actions were commenced in the Supreme Court of the State of New York. Actions brought in several counties in New York state were transferred on defendants' motion to New York County (Manhattan) and consolidated before one especially appointed judge. He in turn directed that discovery in the New York state court cases be coordinated with the Southern District cases. All actions brought in other state courts were either removed and transferred or eventually dismissed.

been filed, trial was commenced in the *SEC* action. The trial lasted until June 21, 1966, and the product of that trial, exhibits and transcripts, was also made available to all of the private plaintiffs.

It is at this point in time that petitioner Reynolds came into the picture. His action was commenced on July 12, 1966, while the *SEC* case was *sub judice* before Judge Bonsal. Reynolds' case was not initiated as a class action, but sought only damages for his own sale of 500 shares of Texas Gulf stock. His was the 94th private action commenced against Texas Gulf Sulphur Company. As had been done with all previous cases brought outside New York, defendants moved on August 31, 1966 to have the *Reynolds* case transferred to the Southern District of New York so that it could be there consolidated with the other pending cases. These cases by then included at least 32 purported class actions, twenty of which claimed to represent persons who sold at the same time as alleged by Reynolds.*

The motion to transfer and coordinate the *Reynolds* case with the New York litigation was vigorously opposed. Reynolds emphasized the individual aspects of his case, such as his age and desire for a speedy trial, and his selection of Utah as a forum. There was no claim advanced at that time that he represented a class of thousands of sellers of Texas Gulf stock. The motion to transfer his

* That is, persons who sold after Texas Gulf's release of April 12, 1964 and before issuance of Texas Gulf's release of April 16, 1964. Mr. Reynolds alleged in his complaint that he placed an order to sell his TGS stock on April 15, 1964. Discovery and trial later revealed he sold on April 16, 1964, after the April 16 release had been issued and its contents communicated to his brokerage firm by the Merrill Lynch private wire and Dow-Jones Broad Tape.

individual case was denied by Judge Ritter, and Texas Gulf's petition for a writ of mandamus to require a transfer was also denied. *Texas Gulf Sulphur Company v. Ritter,* 371 F.2d 145 (10th Cir. 1967).

Thus the *Reynolds* case, alone among the 94 cases that had then been brought with respect to the Timmins discovery in the federal courts, remained outside the Southern District of New York. In the wake of the Tenth Circuit decision affirming the refusal to transfer, three more actions against Texas Gulf, including the *Mitchell* action, were also filed in the District of Utah, and consolidated for trial with *Reynolds.*

It was only after the denial by Judge Ritter of the transfer motion that Reynolds amended his complaint to allege that it was brought on behalf of a class of persons "similarly situated to" Reynolds.* On January 27, 1967 Reynolds moved pursuant to Rule 23 to have his action declared a class action. Following hearing of the motion, Judge Ritter entered an order finding that petitioner had failed to sustain the burden of producing facts to justify the determination that his action was a proper class action. The court's order noted the extent of the litigation in the Southern District of New York and that such actions had been assigned to a single judge for discovery and trial. The court held that:

> "If the various private suits are to be concentrated for trial in a single forum, they should be concentrated in the Southern District of New York and not in this District."

* Our references to petitioners in the discussion of the class action questions should be understood to refer only to the *Reynolds* case. The *Mitchell* case did not purport to be a class action.

Judge Ritter also noted that substantial difficulties would be encountered in attempting to manage the proposed class action from the District of Utah. Subsequently, on October 12, 1967, Judge Ritter dismissed the class allegations in the case of *Karlson* v. *Texas Gulf*, one of the subsequent actions brought in the District of Utah, with Reynolds' lawyer as counsel for the Karlsons.

On August 19, 1966, Judge Bonsal had ruled that Texas Gulf had not violated §10(b) of the Securities Exchange Act when it issued the release of April 12, 1964. The SEC appealed from that decision, and these appeals were argued before the Second Circuit in March of 1967. Not until approximately 18 months later, in August of 1968, did the Second Circuit announce its *en banc* determination. Meanwhile the *Reynolds* case and the three others pending in the District of Utah proceeded to trial, and plaintiffs in two actions in the Southern District of New York entitled *Cannon* v. *Texas Gulf* and *Green* v. *Texas Gulf* (subsequently consolidated and referred to as the *Cannon* case) moved on November 8, 1967, for a determination that their actions could be maintained as a class action under amended Rule 23. On November 27, 1967, this motion was adjourned *sine die* pending the outcome of the appeal in the *SEC* case. Thereafter, upon the reversal in part by the Second Circuit, plaintiffs in *Cannon* renewed their Rule 23 motion before Judge Bonsal and it was argued on October 30, 1968. The SEC filed a brief *amicus curiae* supporting the *Cannon* plaintiffs' motion.

Upon the hearing of the motion, Judge Bonsal indicated that a class action might not be appropriate in cases where management of a class action would entail substantial effort, expense and time, and where plaintiffs could not show

a substantial chance of recovery. This was the view expressed in then recent Southern District decisions, and the record in the *SEC* case did not contain any evidence of intentional wrongdoing which, the Second Circuit had indicated, was the predicate for any private recovery. Counsel for plaintiffs in eight of the cases before Judge Bonsal also appeared and argued against the maintenance of a class action at that point. In response, the moving parties requested further discovery. The District Court granted this request, and depositions were taken by the New York class action plaintiffs in December of 1968.

Thereafter Judge Bonsal, in an opinion dated March 20, 1969, based on intervening Second Circuit decisions that indicated that the possibility of success was not a factor to be considered in determining whether an action was a proper class action, conditionally granted the *Cannon* motion for a class action. (Rule 23(c)(1) provides that all class actions may be conditional). The class was defined to consist of all persons who sold Texas Gulf stock on April 13, 14, 15 and up until 10:55 A.M. E.S.T. on April 16, in alleged reliance upon Texas Gulf's press release of April 12, 1964. *Cannon* v. *Texas Gulf Sulphur Co.*, 47 F.R.D. 60 (S.D.N.Y. 1969). The 10:55 time was declared the cut-off point because it was then that the information concerning the second press release was received in every brokerage house in the country and was available to all buyers and sellers of TGS stock. After that time, the court felt, the questions of whether individual sellers had actual knowledge of information contained in the second press release were too varied to constitute common questions of law and fact. The common issues did not predominate over individ-

ual issues, as required by amended Rule 23(b)(3). See generally Judge Bonsal's opinion in *Cannon* v. *Texas Gulf Sulphur Co.*, 53 F.R.D. 216 (S.D.N.Y. 1971).

Prior to entry of the court's order defining the class, the class action plaintiffs proceeded with discovery through interrogatories and depositions in attempts to identify the class members. At the same time defendants brought on motions for summary judgment in all the private actions pending before Judge Bonsal in the Southern District, which motions were argued on June 12, 1969. The summary judgment motions were granted in part and denied in part in an opinion dated October 31, 1969. *Astor* v. *Texas Gulf Sulphur Co.*, 306 F. Supp. 1333 (S.D.N.Y. 1969). To the extent the motions were denied they nevertheless had the result of simplifying the issues. Texas Gulf, however, remained a defendant in the *Cannon* class action, and the formal order declaring that action to be a class action was signed on November 10, 1969.

The *Reynolds* case and three other cases had gone to trial before Judge Ritter in the District of Utah, sitting without a jury, on April 29 through May 2, 1968. Judge Ritter himself did not announce his decision in favor of the plaintiffs in three of the four cases until September 11, 1969, sixteen months after trial. On October 13, 1969, more than a month after the Utah District Court had rendered its decision on the merits in favor of Reynolds, petitioner sought again to have the *Reynolds* action declared a class action. (The *Karlson* case tried before Judge Ritter was also commenced as a class action and plaintiffs therein were represented by the same counsel who represented Reynolds. But after the decision for defendants in that case there

was no attempt made to declare it a class action.) At this time, there were approximately 90 actions pending in state and federal courts in New York, and *Cannon* v. *Texas Gulf* had been declared to be the appropriate class action representing alleged reliance sellers. Even so, Judge Ritter accepted lengthy briefs and heard oral argument from both sides, and also permitted a New York attorney whose case had not been declared to be the class action in the Southern District of New York to appear *amicus curiae* to urge that the *Reynolds* case be declared a class action. This, of course, took place after the court had announced its decision on the merits in favor of Reynolds. Judge Ritter denied the new motion in an opinion dated January 13, 1970, which refers to the earlier motions and decisions and reaffirms the earlier determination that if the suits were to be concentrated for trial in a single forum, that forum should be the Southern District of New York.

While Reynolds unsuccessfully appealed this ruling to the Tenth Circuit, plaintiffs in *Cannon* were involved in the long and arduous process of locating the members of the class so that they could be given individual notice. Following identification through computer print-out sheets produced by the New York Stock Clearing Corporation on a deposition in May of 1969, some 165 brokerage houses which handled purchases and sales of Texas Gulf stock were required to identify their customers, pursuant to notice and court order of December 29, 1969. The compilation of this information took many months and the difficulties were compounded by the reluctance of several brokerage houses to search their records. After two further orders of the court directed to the brokerage houses, dated June 5, 1970 and July 22, 1970, a mailing list was compiled

from the brokerage house records and from correspondence in the files of Texas Gulf, the SEC, and various private attorneys. This list was filed in the Southern District of New York on November 19, 1970. Notice was mailed to the more than 1600 persons so identified on or prior to November 30, 1970, and this notice provided that requests for exclusion from the class were to be filed by January 15, 1971. By this latter date, the *Cannon* plaintiffs had moved for consolidation of all separately brought claims alleging reliance upon the April 12, 1964 press release, and this procedure was carried out by an order dated February 19, 1971.

At the same time, discovery and other pre-trial procedures on the part of both plaintiffs and defendants were continuing. In addition, on September 3, 1970, plaintiffs in two cases* moved for summary judgment on two grounds: (1) that the evidence as a matter of law established liability of Texas Gulf to the class; (2) that defendants were collaterally estopped by virtue of the decision of the Utah District Court in the *Reynolds* case and of the Second Circuit Court of Appeals in the *SEC* case. That motion was argued before Judge Bonsal on September 14, 1970, and was denied in companion opinions rendered February 5, 1971. *Cannon* v. *Texas Gulf Sulphur Co.,* 323 F.Supp. 990 (S.D.N.Y. 1971) and *Fink* v. *Coates,* 323 F.Supp. 988 (S.D.N.Y. 1971). In denying collateral estoppel effect to the *Reynolds* judgment, Judge Bonsal noted that application of collateral estoppel was within the discretion of the

* The *Cannon* plaintiffs and the same New York plaintiffs who had appeared *amicus curiae* in the District Court of Utah after the decision there to urge that the *Reynolds* case be declared a class action.

court, set forth the factors militating against collateral estoppel, and pointed out that the Utah court had made "no specific findings of fact or conclusions of law with respect to the crucial issue of *scienter*, thus raising a 'reasonable doubt' as to what was decided" in that action. 323 F.Supp. at 990.

Having failed to obtain his goal of a class action in the District of Utah, petitioner Reynolds finally sought to intervene in the New York proceedings on January 15, 1971. Although he had steadfastly resisted any participation in the New York proceedings from the commencement of his lawsuit on July 12, 1966 until January 15, 1971, and notwithstanding that a favorable judgment had been entered on his claim, he filed a Notice of Appearance in the *Cannon* class action in New York, moved to intervene in the New York proceedings under Rule 24 of the Federal Rules, and further moved to have his counsel appointed lead counsel in the *Cannon* action. The New York District Court rejected the application to intervene on the ground that Reynolds had already recovered a judgment in Utah on the claim he sought to make in New York, and that in addition, he was not a member of the *Cannon* class, as he had sold his Texas Gulf stock after Texas Gulf's April 16 announcement had been published on the Dow-Jones Broad Tape. The court did allow, however, Mrs. Margaret E. Wright, also represented by petitioner's counsel, who fell within the *Cannon* class definition, to appear in the action pursuant to Rule 23(c)(2)(C). Counsel for the *Cannon* plaintiffs, who had participated in the New York proceedings for almost six years, who had discovered the identity of class members, and who had administered the giving

of notice to the class members, were declared lead counsel for the alleged reliance claimants.

In conjunction with his application to intervene in the New York action, Reynolds moved to expand the *Cannon* class definition to include sellers after 10:55 A.M. on April 16, 1964 such as himself. This motion and the similar motions of some New York plaintiffs were denied in an opinion dated June 8, 1971 (53 F.R.D. 216), as they had been denied on several occasions before when made by the *Cannon* plaintiffs (*e.g.*, notice of motion dated October 3, 1968; amended class action order noticed for settlement on November 10, 1969; notice of motion dated November 26, 1969), on grounds which included the lack of common questions of law or fact, the difficulty of giving notice, the difficulties of proving reliance, and the small number of persons selling during this period who had brought suit. No appeal was taken or sought to be taken from that decision.

It is correct, as petitioners state, that defendants moved against the class action status of the *Cannon* case on March 5, 1971. However, that motion was denied by the court, in an opinion dated March 30, 1971 (53 F.R.D. 221), and the *Cannon* case retains its class status. Subsequently, defendants moved by a notice of motion filed November 4, 1971, to strike class action allegations in the thirty-three other alleged class actions now pending in the Southern District. Those motions, which were granted in a memorandum decision filed on December 14, 1971, do not affect the class action status of the *Cannon* case. Reynolds' counsel (including his New York counsel) was given notice of the November 4 motion but did not appear nor submit any papers in opposition.

Thus, as matters now stand:

1. Mr. Reynolds has obtained a favorable judgment for himself individually, but it is not binding upon others;

2. The decision adverse to the plaintiff in the companion case in the District of Utah (*Karlson*) is similarly not binding upon others;

3. A class action is proceeding in the Southern District of New York, unaffected by the Utah litigation, as has been the case since its inception.

## ARGUMENT

### I

**This action was inappropriate for class action treatment.**

It was Rule 23 of the Federal Rules of Civil Procedure that petitioners sought to invoke in the United States District Court for the District of Utah. Yet conspicuously absent from the petition herein is any discussion of the elements of that Rule. Instead, petitioners preface the points in their petition with liberal quotations from Professors Moore, Chaffee and others, and essentially argue that absent persons would have fared better had their case, rather than another case, been declared the class action for the *Texas Gulf Sulphur* litigation.

All of the scholars quoted by petitioners were considering the problems posed by multiple claims and were discussing the "spurious" type of class action under former

Rule 23, and in some instances were proposing methods for coping with multiple claims. This Court and the Advisory Committee which recommended the amendment of Rule 23 in 1966 fully considered the writings of these scholars in arriving at the text of the rule which was ultimately promulgated. Quotations of discussions of general concepts, written long before amended Rule 23 came into existence, are of little assistance in evaluating the issues posed by the present petition.

This Court set forth in Rule 23 the elements to be considered by the District Courts in making determinations as to whether a particular case is to be prosecuted as a class action. The prerequisites to any class action are set forth in Rule 23(a), and if these prerequisites are present, the District Court is next required to determine whether or not the additional elements of one of the subdivisions of Rule 23(b) are present, in this type of case the elements of Rule 23(b)(3). Rule 23 further specifies the procedures to be followed by the District Courts in considering motions for class action treatment and in managing class actions.

The rulings of the District Court of Utah were completely in accord with Rule 23, and indeed, no other rulings could have been properly rendered under the Rule. We shall first consider the applicability of Rule 23 with respect to the various attempts by petitioners to invoke it. Thereafter we shall consider in the context of this litigation the other arguments advanced by petitioners.

**A. The Rule 23 motions before trial**

When Judge Ritter denied the defendants' motion to transfer the *Reynolds* case to the Southern District of New

York, it was the only one of more than 50 cases pending in the federal courts involving the Texas Gulf mineral discovery which had not been brought before Judge Bonsal in the Southern District of New York for coordinated discovery and trial. It was the only federal case pending outside the Southern District of New York when petitioner Reynolds amended his complaint and sought by motion of January 27, 1967 to declare his case a class action. Utah was hardly a "center" of the Texas Gulf litigation as petitions contend (Pet., p. 6).

Upon the motion, the District Court in Utah entered an order finding that:

> "plaintiff failed to sustain the burden of producing facts which would justify the determination by the court that the [Reynolds] action is a proper class action as required by Rule 23 of the Federal Rules of Civil Procedure, as amended."

Specific findings with respect to the factors mandated by this Court to be considered under Rule 23(b)(3) were made by the District Court.

Judge Ritter properly took notice of the extent and nature of the *Texas Gulf* litigation in denying the motion as directed by Rule 23(b)(3)(B).* Similarly, Judge Ritter specifically ruled upon the desirability or undesirability of concentrating the litigation of the claims in Utah, as directed by Rule 23(b)(3)(C). At argument, he noted the

* Reynolds' vigorous opposition to the earlier transfer motion had indicated his interest in controlling the prosecution of his individual action, and the number of other suits brought indicated the interest of others in prosecution of their separate actions. The District Court, however, made no express finding on this element mentioned in Rule 23(b)(3)(A).

impossible situation of having class suits proceeding in different jurisdictions with conceivably conflicting results and specifically found that:

> "numerous actions involving similar issues of fact and law have heretofore been filed and are now pending before the United States District Court in the Southern District of New York, 32 of which actions purport to be class actions."

He further found in accordance with the mandate of Rule 23(b)(3)(C):

> "That if the various private suits are to be concentrated for trial in a single forum, they should be concentrated in the Southern District of New York and not in this district [Utah]."

The District Court also addressed itself to Rule 23(b)(3)(D) and found that "substantial difficulties would be encountered in attempting to manage the proposed class action from this District".* The testimony before the court at the time this conclusion was made established that the stock transfer books of Texas Gulf were in New York City, that it would be necessary to go to the stock exchanges which are located in New York to determine the clearing house firms, and then go to the brokerage firms who were involved in trading Texas Gulf shares to determine for whom all of the various transactions were made. In addition, the defendants and the corporate records of Texas Gulf were located in New York and the *SEC* trial and all

---

* Petitioners quote Judge Ritter's concern with managing a lawsuit involving persons who sold 691,000 shares of stock. Rule 23(b)(3)(D) requires the trial court to consider the difficulties likely to be encountered in the management of a class action, and Rule 23(b)(3) states that a class action is to be declared only if it is "superior to other available methods for the fair and efficient adjudication of the controversy."

the attendant discovery had there taken place. Thus, contrary to petitioners' suggestions that Judge Ritter failed to make necessary findings, the specific subdivisions of Rule 23(b)(3) were considered by him and findings made that the *Reynolds* case was not the proper case for class action treatment.

Denial of class action status to this case was correct.

**B. The motion for class status after the decision in favor of petitioners was required to be denied by the explicit language of the Rule.**

Petitioners also suggest that the District Court was in error in denying the motion to declare a class action after the court had announced in September of 1969 its decision in favor of petitioners. But Rule 23(c)(1) specifies the time when the District Court is to determine whether or not an action is to proceed as a class action, and it specifically prohibits the creation of a class action at that late point, after a decision has been rendered:

> "As soon as practicable after the commencement of an action brought as a class action, the court shall determine by order whether it is to be so maintained. An order under this subdivision may be conditional, and may be altered or amended *before the decision on the merits.*" (Emphasis added.)

The District Court below followed the procedure specified in the Rule in entering its order on February 6, 1967, a little more than three months after the amended complaint containing class allegations was filed. This case was pre-tried and tried on the basis of its being an individual suit.

That was the posture of the case when a memorandum of the court's determination was filed September 11, 1969. This was the "decision on the merits,"* and after it was rendered, there was no procedural basis for the backdoor renewal of the class action motion on October 13, 1969, when petitioner Reynolds, aided by persons whose New York action had not been denominated as the class action, again sought to have Judge Ritter declare the *Reynolds* case a class action.

The Advisory Committee's Notes make it clear that one of the principal purposes of Rule 23 was to prevent "one-way" intervention after a decision on the merits, stating explicitly that "one-way intervention is excluded." 39 F.R.D. 106. Petitioner, however, points to the language in Rule 23(d) which provides for "Orders in conduct of Actions" and states that these orders "may be altered or amended as may be desirable from time to time". (Pet., p. 20) As the language of the Rule itself and the Advisory Committee's Notes indicate, the orders referred to are those necessary to the fair and efficient conduct of an action which has been determined, at least conditionally, to be a class action. That subdivision does not apply unless a class action has been properly declared. The suggestion by petitioners that the general language of subdivision (d) should prevail over the express language of subdivision (c) and the expressed intention of the revisers of the Rule is simply without merit.

* At one point in their brief petitioners suggest that their motion was made before the "decision on the merits" because it was "before entry of judgment" (Pet., p. 20). Elsewhere, petitioners acknowledge that the Utah District Court announced its opinion "resolving the merits" on October 17, 1969 (Pet., p. 6). The decision on the merits was announced even earlier, on September 11, 1969.

The motion to declare a class action after the decision on the merits should not, under the Rule, even have been entertained. The denial of class action status after the decision on the merits was correct.

### C. The rulings below were required by the provisions and purposes of amended Rule 23.

The rulings below were clearly in accord with both the letter and spirit of Rule 23 as revised in 1966. Petitioners argue for different results, but rely upon inapposite authorities and misguided reasoning.

The issue before the District of Utah was not whether any class action at all was appropriate, but whether the *Reynolds* case should have been *the* class action. Petitioners argue that the "class" would be better served were the *Reynolds* case now to be declared *the* class action. This argument, of course, has the advantage of hindsight, since *Reynolds* has, as of this point, obtained a favorable judgment; but this fortuity cannot be used to bring about a result so contrary to the law, to sound policy, and to the purposes of the amended Rule. To the same arguments, the Tenth Circuit concluded that "the trial court has wisely exercised its discretion" (80a).

In discussing the issues, petitioners have so mixed together different types of class actions and the authorities applicable to the Rule prior to its amendment, that a totally distorted and indeed unintelligible legal discussion emerges. This fact is evidenced in several different aspects of petitioners' argument.

### 1. *The authorities under former Rule 23 do not provide a basis for now declaring the* Reynolds' *case to be a class action.*

For their argument that the *Reynolds* case should now be declared a class action on behalf of absent persons, and that such persons be given the benefit of the *Reynolds* judgment, petitioners cite *Supreme Tribe of Ben Hur* v. *Cauble*, 255 U.S. 356 (1921). That case is supposed authority for the proposition that the judgment in the *Reynolds* case includes the class although there has been no prior notice.* However, it is clear that the *Ben Hur* case did not involve a Rule 23(b)(3) type of case, or as it was then called, a "spurious" class action which was no more than a device for permissive joinder. Rather, the *Ben Hur* case was the so-called "true" class action now encompassed by Rule 23 (b)(1), and the case is so discussed in the Advisory Committee Notes (39 F.R.D. at 100). *Ben Hur* involved a claim of several parties with respect to a single fund, and its appropriateness for class status was based on the fact that any decision in that lawsuit would necessarily affect the interests of all other parties ("the class"). This Court there held that *res judicata* would apply in that type of case even without prior notice to the class.

In amended Rule 23(c)(3), which discusses formulation of judgments in all categories of class actions, the holding in the *Ben Hur* case is reaffirmed for that type of case. Thus, the first sentence of that subdivision states:

"The judgment in an action maintained as a class action under subdivision (b)(1) or (b)(2), whether or

* This question is not the same as whether the New York court should grant collateral estoppel effect to the *Reynolds* case in the actions pending there. In *Fink* v. *Coates*, 323 F. Supp. 988 (S.D. N.Y. 1971), the court exercised its discretion and denied such a motion.

not favorable to the class, shall include and describe those whom the court finds to be members of the class."

It is the second sentence of amended Rule 23(c)(3) which applies to the instant type of case—a case falling within subdivision (b)(3):

> "The judgment in an action maintained as a class action under subdivision (b)(3), whether or not favorable to the class, *shall include and specify or describe those to whom the notice provided in subdivision (c)(2) was directed*, and who have not requested exclusion, and whom the court finds to be members of the class." (Emphasis added.)

The *Ben Hur* case has no application here.* So, in the instant case, where no notice was given out, there would be no warrant for holding the judgment included others, just as there would be no warrant for holding that the judgment in the *Karlson* case precluded maintenance of actions by members of another purported class.**

---

* Petitioners' citation to other authorities such as *Smith* v. *Swormstedt*, 16 How. [57 U.S.] 288 (1853) and RESTATEMENT, JUDGMENTS ¶86, Comment *h* (1942), are similarly inapposite. These authorities, all written long before the Rule 23 amendment in 1966, refer to true or hybrid class actions, not the spurious class action, or permissive joinder device, which as modified by amended Rule 23 in 1966, is involved in this case.

** The case of *Karlson* v. *Texas Gulf* was also brought in the District of Utah, and it too purported to be a class action. More than 2,000,000 shares of Texas Gulf stock were sold over the New York Stock Exchange by persons who, like Karlson, had not been informed of Texas Gulf's initial drill hole in Canada. Many of them have brought suits which are presently pending in the Southern District of New York. One can imagine the hue and cry which would arise if, after the adverse decision on the merits in the District of Utah, a class action had been declared and all of those persons were declared to have been barred by the Utah judgment. Respondents have never sought to bar persons with pending suits on the basis that the *Karlson* trial determined their rights. While petitioners' counsel claims he has litigated the rights of the class (Pet., p. 8), he now makes no such claim with respect to the *Karlson* case which he also commenced as a class action.

As the Advisory Committee states, one of the primary purposes of the amendment of Rule 23 was to prevent "one-way intervention" in so-called "spurious" class actions. The Advisory Committee stated that "under proposed subdivision (c)(3), one-way intervention is excluded; the action will have been early determined to be a class or non-class action," and in the former case, the judgment, whether or not favorable, will include the class. While prior to the 1966 amendment certain courts and commentators were tolerant of one-way intervention, the Advisory Committee took a contrary stand, in line with equally impressive precedent. 39 F.R.D. at 105-106.

### 2. *The prosecution of simultaneous class actions would have been improper.*

Petitioners also suggest that simultaneous class actions should have been allowed to proceed in New York and Utah at the same time, and that if this had occurred, the "class" would now be rewarded with the fruits of Reynolds' victory. Both the factual and legal bases for this argument are unsound.

To support their argument that two actions on behalf of a class should proceed simultaneously, petitioners rely upon cases decided under former Rule 23, before its amendment in 1966. Petitioners again fail to appreciate the distinctions between the "spurious" class actions under old Rule 23 and the type of class action under Rule 23(b)(3) of the amended Rule. A spurious class action under former Rule 23 was a permissive joinder device (see, *e.g.*, 3 Moore, Federal Practice ¶¶23.10, 23.12 (2d ed. 1963)), and the judgment "would extend only to the parties including

intervenors", and "was supposed *not* to adjudicate the rights or liabilities of any person not a party." Advisory Committee Notes, 39 F.R.D. 98, 99. (Emphasis added.) Under the old Rule, notice did not go out to persons who did not appear, and non-parties in these spurious class suits were not bound by the judgment. Thus cases such as *Partridge* v. *Martin*, 102 F.2d 284, 288 (8th Cir.), *cert. denied*, 307 U.S. 644 (1939), explain that two class suits could co-exist because neither would render an adjudication binding on absent persons, as distinguished from the *Ben Hur* type case of a true class action.

However ,under amended Rule 23(b)(3), all members of the class must receive notice and be given the opportunity to exclude themselves from the action; persons who do not request exclusion are bound by the judgment, whether favorable or unfavorable. One of the primary purposes of the new Rule was to avoid a multiplicity of multi-party suits. To allow two such actions, with a duplication of the necessarily heavy burdens of administration and management, would only be destructive of the ends sought to be obtained by the Rule. Moreover, to have more than one class action, with notices to the same individuals from separate courts advising them that they were represented in two different actions on the same claim, would engender hopeless confusion and disrespect for the judicial process. The possibility of different results from different courts binding the same individual could compound the problem.

Petitioners also urge that the policy against multiple lawsuits and the philosophy behind the Multidistrict Litigation Act (28 U.S.C. §1407) suggest that the *Reynolds* case should be maintained as a class action. However, it

is not respondents but petitioners who have brought about multiple litigation in different forums in this case. As set out above, respondents made every effort to have all of the cases transferred to the most convenient forum, New York, and to have all the federal cases consolidated in the Southern District of New York. Petitioner resisted the motion to transfer his action to New York where it could have been coordinated with the pending litigation. Instead he sought to prosecute his own action. Moreover, his urging that two class actions should proceed separately is directly contrary to the likely result of any action by the Judicial Panel on Multidistrict Litigation.

Indeed, Rule 23 cannot prevent the existence of separate individual suits, if persons such as petitioner desire them. A class action cannot insure that there will be only one trial. Rule 23 provides the option to class members to exclude themselves from the class, and to prosecute their separate actions. This has occurred in the New York proceedings, and it is certainly possible that in every class action situation, individuals desiring to maintain their own suits may obtain a judgment before a class action, with its attendant notice and administration problems, can be concluded. It is the very fact that the *Reynolds* case was not a class action that enabled it to reach judgment before the declared class action. The entire purpose of the Rule would be subverted, if, as here, a party obtaining an individual verdict in his favor could thereafter convert it into a class action.

### 3. *Difficulties inherent in managing a class action inevitably entail time-consuming procedures.*

Petitioners assert that the lower courts have ignored procedures which could have significantly shortened the duration of this litigation. But the length of time consumed results from the fact that the *Cannon* case is a class action, not an individual suit, and as such involves complex administrative problems. In New York, after all parties awaited the Second Circuit decision in the *SEC* action, a great deal of time was expended in discovery proceedings of brokerage houses, receiving and compiling names of potential class members, preparing and mailing notices, answering responses, and coordinating numerous other cases with the class action for trial purposes. These problems, particularly in dealing with brokerage houses, would have been exacerbated and even more time would have been expended if a class action had gone forward in Utah, and if as Rule 23 requires, notices had been sent out from the District Court in Utah prior to trial.

Petitioners also intimate that respondents have engineered "interminable delays", citing in footnote 6 on page 7 of their petition, 15 reported opinions in the *Texas Gulf* litigation. As this Court should be apprised from the pending petitions in Nos. 71-327, 328, 346, 347 and 421, the issues raised by this litigation are of first impression. Five reported decisions are in the *SEC* case, four in the Utah cases (including the decision upon respondents' attempt to transfer the *Reynolds* case to New York), one in Illinois upon a transfer motion, and five decisions on procedural and substantive motions brought by both plaintiffs and defendants in the coordinated New York proceedings. The

"delay" includes the 18 months the Second Circuit held *sub judice* the SEC's appeal and the time necessary to conduct the extensive discovery to ascertain and notify the class. All things considered, the litigation has been expeditiously processed, and any delay is the inevitable consequence of mammoth, landmark proceedings.

But speed is not and should not be the sole or determinant factor in considering the problems posed by class actions. The Advisory Committee's approach was not that "judicial efficiency is considered paramount." (Pet., p. 16). The Advisory Committee has cautioned that Rule 23 is to be used "without sacrificing procedural fairness or bringing about other undesirable results." 39 F.R.D. at 103. The alternatives suggested by petitioners would achieve just the opposite effect from that intended by the drafters of the Rule.

**D. Petitioners' forays outside their chosen forum.**

***1. The inapplicability of the Multidistrict Litigation Act.***

Petitioners complain that their belated attempt to invoke the procedures of the Judicial Panel on Multidistrict Litigation were ignored by the Court of Appeals for the Tenth Circuit. (Pet., p. 21). In a footnote they acknowledge that there is a "conceptual problem" because 28 U.S.C. §1407 deals exclusively with pretrial proceedings. The problem exists because petitioners only sought to invoke that statute after pretrial proceedings had been completed, after a trial had been completed, and after an appeal to the Tenth Circuit had been fully briefed and argued.

Not only was petitioners' timing late, but also their plea was addressed to the wrong body. 28 U.S.C. §1407(c) provides that proceedings for the transfer of an action under this section can be initiated by the Judicial Panel on Multidistrict Litigation upon its own initiative or by "motion filed with the panel by a party in any action * * *." Petitioners filed no such motion with the Judicial Panel, and they can hardly complain of inaction by that body in their petition here.

### 2. *Petitioners' attempts to participate in the New York class action proceedings.*

It was not until 1971, four and one-half years after his complaint was filed, and a year after judgment had been entered in his favor in the District of Utah, that petitioner first saw fit to attempt to bring his suit into the New York courts and for his counsel to assert his claim to lead counsel status in the New York proceedings.

Reynolds of course by this time had obtained a judgment on his claim in the District of Utah, and it is difficult to see how in those circumstances he could properly intervene in the New York cases. Moreover, he was not within the class as defined in the *Cannon* case, having sold after 10:55 on April 16. His counsel was permitted to appear pursuant to Rule 23(c)(2)(C) on behalf of one of the members of the *Cannon* class who claimed to fall within that class action definition, but lead counsel status was granted to those who had represented the class from the beginning of the New York cases. Of course, any grievance Reynolds may have from denial of those motions can be taken up in the federal courts in New York.

Nevertheless, some response to the attacks on Judge Bonsal should be made. He has been coordinating this complex and difficult litigation for six years. All the substantive matters which counsel for petitioner Reynolds sought to raise by intervening in the New York proceedings had been fully briefed and argued by counsel legitimately appearing in that court. While we do not agree with all of the decisions reached by that court, they were arrived at after full and fair hearing. Judge Bonsal listened patiently to the attacks made by petitioners' counsel upon his rulings on February 10, 1971.

Petitioners also assert that the New York court was in error in limiting the class to pre-10:55 sellers. This again is a problem for the New York courts. But passing that for the moment, there is a substantial difference between those who sold TGS stock prior to the company's release of April 16, 1964, and those who sold after that release was issued, such as Reynolds. Even Judge Ritter stated in his opinion on petitioners' final class motion, that "there can be no question but that there were differences in the kinds and degrees of reliance by the persons to whom the April 12 release was addressed as demonstrated by plaintiffs Reynolds, Mitchell and Stout", all of whom had sold after 10:55 on April 16th. Persons such as Reynolds and Mitchell are in an entirely different position from those who sold during the period *before* the April 16 release. Even if some late sellers may be able to maintain individual actions, it by no means follows that a class action is appropriate. In any event, review of that decision lies elsewhere than by this petition.

## II

**The courts below correctly refused petitioners' claim for counsel fees.**

The District Court refused to award attorneys' fees and the Court of Appeals affirmed, finding no authority for such an award in a private damage suit. That decision was in all respects correct.

Attorneys' fees are recoverable only in certain situations, such as where a statute explicitly so provides (see *Fleischmann Distilling Corp.* v. *Maier Brewing Co.*, 386 U.S. 714 (1967)), or where a fund has been created for the benefit of a group of persons and it would be inequitable to require the person whose suit created that fund to absorb all of the attorneys' fees, giving the other parties a windfall. (*E.g.*, *Sprague* v. *Ticonic National Bank*, 307 U.S. 161 (1939)). Petitioners' citation of *J. I. Case Co.* v. *Borak*, 377 U.S. 426 (1964) and *Mills* v. *Electric Autolite Co.*, 396 U.S. 375 (1970) are inapposite here, for those cases are based on the same proposition stated in *Sprague*. Both *Borak* and *Mills* were derivative suits on behalf of corporations, and the corporations which had received the benefits were required to compensate plaintiffs' attorneys for their efforts in conferring those benefits. Where there has been no benefit to the corporation, attorneys' fees are denied in actions under Rule 10b-5. *Saltzman* v. *Technicolor Inc.*, 51 F.R.D. 178, 185 (S.D.N.Y. 1970). The instant case has been of no benefit to Texas Gulf Sulphur Company. Far from creating a fund for Texas Gulf which should be shared with petitioners' attorneys, petitioners, who profited

from their trading in Texas Gulf stock and received speculative profits as damages besides, have caused Texas Gulf and its stockholders to incur substantial expense.

## Conclusion

It is respectfully submitted that the courts below were correct in concluding that petitioners should be left to the rights which they sought to pursue on their own behalf in Utah. Reynolds did not go to trial as a champion of the class and his counsel did not, prior to January 1971, seek to coordinate his case with those in the New York courts. Having apparently determined that this individual course was not as economically profitable as desired, petitioners seek to reverse all the decisions they made four and five years ago—indeed decisions which they persuaded the federal courts to then make. The federal judiciary is otherwise attending to the claims of allegedly aggrieved parties, and the relief here sought is both unnecessary and unwise.

Respectfully submitted,

ORISON S. MARDEN
*Attorney for Respondents*

CALVIN A. BEHLE
KEITH E. TAYLOR
PARSONS, BEHLE & LATIMER

P. B. KONRAD KNAKE
THOMAS MCGANNEY
JEFFREY A. BARIST
W. NEIL THOMAS III
WHITE & CASE
*Of Counsel*

December 20, 1971

SUPREME COURT, U. S.

FILED

JAN 8 1972

E. ROBERT SEAVER, CLERK

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1971

No. 71-693

GEORGE GORDON REYNOLDS AND WALTER A. MITCHELL,
*Petitioners,*

v.

TEXAS GULF SULPHUR CO. AND CHARLES F. FOGARTY,
*Respondents.*

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

## REPLY BRIEF FOR PETITIONERS

PARKER M. NIELSON
320 Kearns Building
Salt Lake City, Utah 84101
*Attorney for Petitioner Reynolds*

ROY G. HASLAM
72 East 4th South Street
Salt Lake City, Utah 84111
*Attorney for Petitioner Mitchell*

## TABLE OF CONTENTS

ARGUMENT ..... 2
CONCLUSION ..... 9

### Cases Cited

Astor v. Texas Gulf Sulphur Co.,
306 F. Supp. 1333 (S.D.N.Y. 1969) ..... 8

Dolgow v. Anderson, CCH Fed. Sec. L. Rep.
¶93, 249 (E.D.N.Y. October 21, 1971) ..... 9

Esplin v. Hirschi, 402 F. 2d 94
(10th Cir. 1968) *cert. denied* 394 U.S. 928 (1969) ..... 8, 9

Heddendorf v. Goldfine,
169 F. Supp. 915 (D. Mass. 1958) ..... 6

Marcus v. Textile Banking Co.,
38 F.R.D. 185 (S.D.N.Y. 1965) ..... 5

Norman v. McKee,
290 F. Supp. 29 (N.D. Cal. 1968) ..... 6

Webster Eisenlohr v. Kalodner, 145 F. 2d 316
(3rd Cir. 1944) *cert. denied* 325 U.S. 867 (1945) ..... 5

### Statutes and Rules Cited

28 U.S.C. § 1407 (b) ..... 2

Rule 23 (c), Fed. R. of Civ. P. ..... 6, 8, 9

Rule 23 (d), Fed. R. of Civ. P. ..... 6

Rule 23 (e), Fed. R. of Civ. P. ..... 6

### Authorities Cited

Haudek, W., *The Settlement and Dismissal of Stockholders' Actions*, 22 Sw. L. J. 767 (1968) ..... 5

N. Y. Times, Dec. 31, 1971, at 27, col. 1 ..... 4

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1971

No. 71-693

---

GEORGE GORDON REYNOLDS AND WALTER A. MITCHELL,

*Petitioners,*

*v.*

TEXAS GULF SULPHUR CO. AND CHARLES F. FOGARTY,

*Respondents.*

---

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

---

## REPLY BRIEF FOR PETITIONERS

---

Petitioners George Gordon Reynolds and Walter A. Mitchell reply to the Brief for Respondents in Opposition, advising the Court in particular of events which have transpired subsequent to the filing of the Petition and which underscore the national importance of the matters this case presents.

## ARGUMENT

### —A—

Respondents urge this Court to ignore the implications of the related New York proceedings, as if a primary function of this Court was not the supervision of a unified federal judiciary, and as if the Petition were not addressed to that very problem. We submit that this Court not only can, but should, resolve such inter-jurisdictional conflicts in the interest of assuring a truly functional federal system. Indeed, section (b) of the Act creating the Multi-District Panel[1] (quoted at Pet. 4) clearly mandates that "the Chief Justice of the United States" *shall* exercise influence in such matters, if there could be any doubt, and while the Southern District of New York is assuredly a respected court Respondents suggestions that it should be the *final* arbiter of either class action or securities law matters is an unwarranted extension of the jurisdiction of the trial court. The parallel New York proceedings are also not matters beyond the record, for they are in evidence in the affidavits of Respondents, who considered them to be proper for consideration by the lower courts when they were urging the dismissal of Reynolds' class allegations but somehow improper now that the dismissal thus solicited is presented for review. Moreover, many of these matters are the subject of published opinions of which this Court may take notice.

### —B—

The dilemma presented by the Petition is whether what Respondents agree is now obvious by a process of hindsight,

---

[1] Respondents urging that Reynolds was tardy in suggesting use of the Multi-District Panel ignores the fact that the legislation creating the Panel was not adopted until *after* the *Reynolds* case went to trial. We nevertheless submit that its procedures should have been applied to cases then in progress and made that suggestion to the Court of Appeals—which was the only court appropriate for such a suggestion at that time.

could not have been secured through a proper application of Rule 23's procedures as a matter of foresight; or, if the Advisory Committee did not visualize procedures which would have secured these benefits, in all events, without regard for either foresight of hindsight. It is always easy, in lieu of logic, to answer an argument concerning faulty procedures with the hindsight cliché advanced by Respondents, but that is not a solution to the problem. If this dilemma is not resolved by this Court, advanced age may well prove to be the common denominator of all class proceedings, for other defendants in large class action claims will be quick to follow the blueprint for delay of the Respondents herein. Reynolds did, as Respondents have suggested, select the Utah forum in the belief that it could resolve his claim with greater dispatch, but why is not that same consideration of common interest to the entire group of absentees?

–C–

The spectre of confusion flowing from two class actions is a contrived one which will be remedied, not created, if the procedures specified in the Rule are implemented. Furnishing the simple notice affording all absentees the election of participating or "opting out" as specified by the Rule, in lieu of the "Big Brother" approach of Respondents in which that election is already made for them, will result in all class members being quickly aligned with the forum of their choice – and the present confusion and delay in the Southern District of New York will be removed. If the objective be an honest judicial system, what can be so repugnant to giving litigants that simple choice, particularly when the Rule itself was calculated to preserve the individual rights of litigants to the maximum extent consistent with the creation of a streamlined judiciary?

—D—

The crises of judicial inefficiency and delay referred to in the Petition continue unabated and are further compounded by intervening events. As all other events have appeared orchestrated by TGS to undercut these proceedings, the Respondents announced in the New York press on December 31,[2] in apparent response to the Petition seeking relief from judicial inefficiency, that they would seek the compromise of the rights of the uninformed absentees in the New York proceedings — apparently without regard for the views of this Court — at a level approximately 20%[3] of that already adjudicated by Reynolds. We are uninformed as to whether counsel for the New York plaintiffs collaborated in making that proposal, though TGS's public announcement suggested that they did, but counsel for Reynolds have already objected to the proposal[4] and Respondents surely know that any faint-hearted compromise[5] of the absentee's rights will inevitably lead to appeals and additional delays in the New York courts. Neither do we know if the New York court approved of TGS's public announcement, though the announcement itself suggested that it did and the record suggests that the compromise was pro-

---

[2] N.Y. Times, Dec. 31, 1971, at 27, col. 1.

[3] The settlement proposal apparently encompasses a mere 364,900 shares of the 691,000 shares which Reynolds claims should be protected, for the announced sum of $2.7 million, or $7.40 per share. We may safely postulate that *all* of the selling shareholders in this group sold at approximately Reynolds price, or less. Thus, calculated at a selling price of $33 per share, and taking the Court of Appeals calculation of damages at the difference between the selling price and $59, together with interest at 6% to the time of judgment, damages under the measure established by Reynolds would be $34.97 per share, or $26.56 in excess of TGS's New York settlement proposal.

[4] The statement at Br. in Op. 14 that counsel for Reynolds did not oppose Respondents motion in the New York proceedings to restrict the class membership is incorrect, for reasons we are confident were unknown to Respondents. On November 16, 1971, counsel for Reynolds

grammed months ago (see footnote 10 at Pet. 14). It would be curious, however, if either the New York counsel or the New York court did participate in such a scheme, alien as it is to the interests of the absentees and at a time when the issues of liability and damages which are the customary ingredients of a compromise are a matter of *res judicata* herein, and yet claim that they "fairly and adequately protect the interest of the class" as the Rule requires. Nevertheless, there is adequate time to obtain an appropriate stay order to permit the work of this Court to be concluded, if the integrity of the judicial system so requires.

The matter of national importance in these subsequent events, which commends the attention of this Court, is that these practices, whether by calculation or happenstance, stand as a mute subversion of the policies of Rule 23. The proposed New York compromise includes but a portion of the group Petitioners claim to represent, which means that the rights of one group (sellers similarly situated with Reynolds and Mitchell) are being sacrificed to obtain a settlement of questionable fairness even to the group it will benefit, or which at

---

requested, in a written document a copy of which was furnished to the court, that "lead counsel" designated by the New York court file appropriate papers opposing Respondents' motion. Because of the outstanding orders discussed at Pet. 7, counsel for Reynolds were disabled from filing any papers in their own right. Despite the request, "lead counsel" failed to oppose Respondents' motions and the announced "compromise" followed immediately.

[5] "[T]he Rule is designed to protect the class against surrender of class rights by a greedy or fainthearted plaintiff . . . ." Haudek, W., *The Settlement and Dismissal of Stockholders' Actions*, 22 Sw. L. J. 767, 776 (1968), citing Webster Eisenlohr v. Kalodner, 145 F. 2d 316, 320 (3d Cir. 1944), *cert. denied*, 325 U.S. 867 (1945); Marcus v. Textile Banking Co., 38 F.R.D. 185 (S.D.N.Y. 1965).

the very least will leave a substantial body of shareholders without any forum in which to present their claims. Whether the case be considered as arising under Rule 23(d) – which Judge Ritter plainly declared was the procedure he was following (App. 36a) – or under Rule 23(c) which Respondents urge that the Petition should have discussed even though its procedures were never invoked by the trial judge – is academic when one considers that *both* subdivisions require notice to the absentees of *every* matter which affects their vital interests. Moreover, Rule 23(e) requires that "notice of the proposed dismissal or compromise be given to all members of the class . . . ." Yet, the holders of approximately 325,000 shares have had their case dismissed, and have yet to receive any notice at all. The trial judge in class proceedings is intended to be the *guardian* of the absentees rights, not a mere arbiter in a game where the rights of the absentees are the pawns. *Norman* v. *McKee*, 290 F. Supp. 29, 32 (N.D. Cal. 1968); *Heddendorf* v. *Goldfine*, 169 F. Supp. 915, 926 (D. Mass. 1958).

Can it be fairly said that a system which produces seven years of delay – and then only the prospect of a substantial subversion of the absentees rights – is progressing in an orderly fashion, or, indeed, that such a system is functioning at all? Respondents do not claim that the seven years of delay were consumed in identifying the class members, nor could they make such a claim, for none of the multiple actions in New York which did not involve class allegations have proceeded with greater dispatch. Moreover, the *Reynolds* case had been tried and was pending on appeal before class action proceedings were ever invoked by the New York court. Had the delay been caused by the class proceedings the discretion the Rule vests in the trial judge was then ignored, for there is nothing in the Rule which prohibits proceeding with the trial of the common issue, as Reynolds has done, while the task of auditing

the brokers records[6] was in progress. The task, in short, is to devise a system which *will* work. The proceedings in New York show that in the context of this case it is not working, and it bears no promise of working unless a more enlightened approach to the class action is directed by this Court.

—E—

Respondents attempt to make light of the prefatory quotes contained in the Petition with their observation that they should not be considered because the Advisory Committee adopted its own philosophy. That argument simply taxes credibility, for the philosophy thus adopted *was* that of the prefatory quotes. Indeed, these citations were taken directly from the Committee notes.

Alternately, Respondents suggest that the Petition is "distorted and . . . unintelligible" because it fails to segregate "spurious," "hybrid," and "true" class actions, and relies instead upon the philosophical writings referred to in the Advisory Committee notes. These arguments are but expressive of the crises in judicial administration that this case represents, for nothing could be as plain as the Advisory Committee's declaration that this confusing and often misleading terminology was to be abandoned in favor of a practical concern for the rights of litigants. Thus, in this case there has been a substantial retreat from the policies the Advisory Committee sought to adopt and a return to many of the policies of the former rule which the Advisory Committee effected to discard. This Court should exercise its supervisory role to restore the intended meaning to the Rule.

---

[6] The task of auditing the brokers records is now completed. Petitioners do not propose to duplicate that work.

—F—

Respondents urging that the *Reynolds* case should not be extended to all persons similarly situated because a companion case involving a shareholder who sold prior to March 27, 1964 (the *Karlson* case discussed at Brief in Opposition, 10, 15, 23) was not urged by Petitioners to be a class action, simply ignores the obvious, for the holding in *Karlson* was given effect, *sub silentio* in *Astor v. Texas Gulf Sulphur Co.*, 306 F. Supp. 1933 (S.D.N.Y. 1969) when the cause of all persons similarly situated with *Karlson* was dismissed on Respondents' motion. Thus, it is Respondents rather than Petitioners who press for a one sided application of the Utah judgments.

—G—

Otherwise, Petitioners and Respondents have many obvious differences over the proper construction and application of the Revised Rule, and though Respondents are critical of our not discussing these elements in the Petition we submit that these are questions beyond the proper scope of a Petition and are appropriate only to the briefs on the merits. It is appropriate to observe, however, that Respondents repeated assertion that Rule 23 was "to prevent 'one way' [7] intervention" (Br. in Op. 20) is a calculated misreading of the Rule which ignores judicial precedent on the subject. The Advisory Committee notes say that *under subdivision (c)* one way interven-

[7] "One way intervention" describes the practice under the former Rule of converting individual actions into class actions after judgment was entered. The *Reynolds* case does not present a "one way intervention" problem, however, for *Reynolds* moved three times, in each instance before judgment, for appropriate orders under Rule 23. Thus, this case represents a review of allegedly erroneous rulings not within the scope of the "one way intervention" problem. See Esplin v. Hirschi, 402 F.2d 94 (10th Cir. 1968) *cert. denied* 394 U.S. 928 (1969).

tion was to be eliminated, but that comment is not relevant to these proceedings because subdivision (c) was never invoked because of the errors by the lower courts. As we pointed out at pages 19-20 of the Petition, the Advisory Committee clearly declared that if there was a defect in notice, absentees might nevertheless participate in a favorable judgment obtained for their benefit, even though the jural relationship subdivision (c) contemplates was not created. Judge Weinstein read the revised Rule in that fashion in *Dolgow v. Anderson,* CCH FED. SEC. L. REP. ¶ 93,249 (E.D.N.Y. October 21, 1971), and the Court of Appeals reversed the dismissal of a class action in *Esplin v. Hirschi,* 402 F.2d 94 (10th Cir. 1968) *cert. denied* 394 U.S. 928 (1969), after the case had been decided on the merits. What Petitioners urge is less in the nature of "one way intervention" than the practices approved in both *Dolgow* and *Hirschi.* Respondents position would effectively mean that class action rulings are exempt from any appellate review, and would be in conflict with both *Dolgow* and *Hirschi.*

## CONCLUSION

Even if the order of filing by the respective plaintiffs was a proper consideration, it must be observed that the Reynolds case is not in any sense a late "arrival." Respondents would speak more accurately if they said that Reynolds was a late starter, for he is not only an early "arrival' but he is the *only* arrival among all of the hundreds of plaintiffs Respondents make reference to. And, if one can start as far back in the pack as Respondents would have this Court believe that Reynolds did, and yet finish so far ahead in a game where the ultimate goal is efficiency, this Court should at least consider if the procedures invoked at the instance of Respondents in New

York are not a subversion of the judicial system, for there is nothing about the Reynolds case which should produce such a paradox.

Respectfully submitted,

PARKER M. NIELSON
320 Kearns Building
Salt Lake City, Utah 84101

*Attorney for Petitioner Reynolds*

ROY G. HASLAM
72 East 4th South Street
Salt Lake City, Utah 84111

*Attorney for Petitioner Mitchell*